WEALTHMATTERS

YOUR PERSONAL GUIDE TO WEALTH CREATION

ISSUE 45
2018

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Ins and outs of testamentary trusts

Testamentary trusts provide asset protection and tax advantages to the beneficiaries of your will when they inherit your estate.

A testamentary trust is a trust established under a valid will, where a nominated trustee will oversee the distribution of assets to a group of beneficiaries.

Types of testamentary trusts

There are two main types of testamentary trusts:

- Discretionary trusts separate the trust to the deceased estate and the trustee has the discretion to distribute capital between a group of beneficiaries nominated in the will.
- Protective trusts are established in the interest of an individual incapable of managing their affairs.

Tax outcomes

The beneficiaries of discretionary trusts should be consulted so the trustee can gain an understanding of their tax profile. This knowledge will enable trustees to distribute their estate to beneficiaries with differing incomes to reduce the tax burden on the total sum.

Consider the following options for getting you started:

- Pay to a child under 18 to get taxed at adult marginal rates and to be eligible for a low-income tax offset up to $445
- Consider tax advantages of those with high personal marginal rates, a partner on lower income, minor children and grandchildren with no or little taxable income and those on the tax-free threshold.

Protecting your assets

Your trust can also be used to protect your assets in the following circumstances:

- Protect super death benefits paid to your beneficiaries that may otherwise be vulnerable for seizure by creditors
- Help beneficiaries in vulnerable financial situations or work in a high-risk environment
- Protect assets in the event a beneficiary's assets are split during a separation

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Risk management strategies for investors

Failing to manage risk may leave you vulnerable to financial hardship if just one investment goes awry.

Successful investors must have risk management strategies so that unexpected market fluctuations do not leave them out of pocket. These risk management strategies will ensure your investment portfolio can withstand losses and continue to generate profit.

Identify risks

Avoid making a regrettable decision by performing a risk assessment before investing. Identify risks associated with the company, industry and type of investment so you can assess whether you can afford the investment if the risks materialise and the worst case scenario plays out.

Diversify

Investing in a diverse range of assets and industries will minimise the impact of one of your investments coming up short. Spread your investments across different asset classes like properties, annuities and fixed interests to create a balanced portfolio where a market downturn in one industry will be compensated for by a profit in another. Consider purchasing a mutual fund or an exchange-traded fund (ETF) to streamline your diversification strategy.

Track your investments

Keep tabs on your finances so you know when it might be time to buy or sell. Organise your target returns according to your asset class and establish an accepted variation range. Consider placing a stop loss order that will sell stocks or ETFs that fall below a certain price. However, you should be cautious of selling off assets prematurely as a brief market dip might explain their loss. If investment's in a certain sector are decreasing in value you may perceive this as an opportunity to buy low and sell high.

Repay your debt with superannuation

You can access your retirement savings early to repay debts that currently have you in a tight financial spot.

The ATO and super providers place strict limits on early access to your super to avoid damaging your quality of life in retirement. Unless you are suffering from severe financial hardship or the Department of Human Services grants you early access on compassionate grounds, you may only access your super early once you reach a certain age.

If you are between your preservation age and 65 years old, you can access your superannuation through a transition-to-retirement (TTR) account-based pension, while continuing to work. You must be a member of an accumulation super fund to be eligible. Move your super funds from the accumulation account to the TTR pension account to gain access to debt repayment funds. You may withdraw four to ten per cent of the commencement value of the TTR pension and can request up to a year's worth of pension payments in advance to meet debt obligations.

Benefits and risks of A-REITs

Australian real estate investment trusts (A-REITs) allow investors to benefit from Australia's thriving property market without the cost of a large deposit.

Weigh up the benefits and risks of A-REITs before deciding to invest in the housing market through your stock portfolio.

How A-REITs work

The resources of investors are pooled together to buy into a range of property related investments. A-REITs typically have a minimum investment of $500, but this may vary.

You can invest in an equity or mortgage A-REIT according to your preference.

- Equity A-REITs are more common and generate a return through the rental payments of the properties they invest in and own. They usually invest in commercial property like offices, shopping centres and hotels and can be specialised or diversified.
- Mortgage A-REITs invest in property mortgages and the interest that is paid back on the loan generates income for investors.

Benefits of A-REITs

A-REITs can provide a range of financial and practical benefits:

- Individuals can invest in large-scale properties they could not afford otherwise.
- Investors are saved the financial burden of large deposits and mortgages.
- A-REITs are managed by investment groups, meaning that individuals may gain the financial benefits of property without the managerial hassle of becoming a landlord.
- A-REITs have high dividend return, at times 90 per cent and above, to attract investors.
- A-REITs are high in liquidity in comparison to traditional property investments due to the fact they are exchanged on the stock market.
- Diversified A-REITs minimise risk

Risks of REITs

A-REITs can also drop in value if their risks materialise. These risks include:

- Volatility in the property market
- Poor management who pay too much for properties or borrow improperly
- The management group fails to find a party to lease space or if rental payments fail in equity A-REITs. This risk is heightened for A-REITs specialising in commercial property due to the rise of e-commerce.

Splitting your super contributions

Super contribution splitting between spouses can result in tax advantages that will help you grow your joint retirement nest egg.

You must meet the eligibility requirements and follow tax rules to avoid incurring penalties from the ATO.

Advantages of super splitting

Some advantages gained from contribution splitting include:

- Gaining access to concessionally taxed or tax-free lump sum super withdrawals earlier
- Increase non-concessional contributions you can make by reducing your total super balance
- Gain earlier access to contributions
- Maximise tax-free pension benefits

Eligibility

Your ATO application will only be deemed valid if:

- The person you are splitting your contributions with is a spouse defined by marriage, a registered relationship or a de facto relationship
- Your spouse is less than the preservation age listed on the ATO or aged between their preservation age and 65 years
- You have not already applied in the financial year where the trustee of your fund has received your application
- The amount of benefits you have used does not exceed the maximum amount that can be split

Types of contributions

You can make taxed splittable contributions (TSCs) or untaxed splittable contributions (USCs).

- Transfer up to 85 per cent of a financial year's TSCs subject to the ATO requirements. Advise your super fund on personal contributions you will claim a tax deduction for. You may also include contributions made for you by your employer and salary sacrifice contributions.
- You can transfer 100 per cent of USCs for the financial year provided that it does not exceed concessional contribution caps for that year.

Time for a super health check

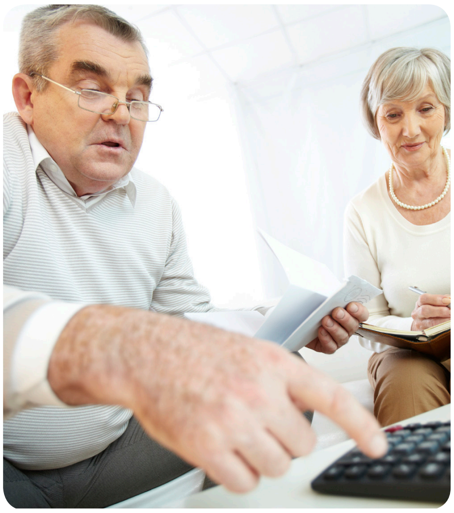
Retirement may seem like a far-off event, but your decisions now will determine how comfortable you are when you stop working.

Checking that your finances are on track is vital to maximising your super, reaping tax benefits and giving your future certainty.

Prioritise a super health check and take the following steps:

Check your fund is right for you

Choosing the right super fund may make thousands of dollars difference to your final super balance. Get educated on the competition, and if a comparison reveals that you are paying more and receiving less, changing funds might be just the ticket. Your new super fund or myGov will provide you with a rollover form to fill out if you switch funds. You will also need to take out new insurance policies and select a new investment option for your new fund and pay fees to close your old account. The fees will include a switching fee and may also include whatever Capital Gains Tax is accrued from selling off your super investments. Check with your current super fund before making the change.



Merge your super

Changing jobs over the years may put you at risk of losing some of your super if your previous employers have set up accounts you have forgotten about. Super balances are eroded by fees in inactive accounts, which is why you should merge your super accounts, so you only pay one set of fees and maximise your return on a single balance. You may chase up inactive super accounts through your current super fund, provided they offer this service, or apply through the ATO.

Salary sacrifice

Put away more money while you can afford to and minimise your tax burden at the same time by making additional, voluntary contributions to your super. Concessional contributions are an effective way to reduce your tax burden by making your taxable income smaller. Voluntary contributions are taxed at 15 per cent, which may help you bring in savings on your tax bill if it is less than your marginal rate. For your pre-tax income, you can make up to $25,000 in concessional contributions. Your non-concessional contributions are capped at $100,000 a year. Track your super contributions as exceeding contribution caps will result in having to pay extra tax.

Reassess your investment strategy

Check in on your investment strategy regularly as your shifting financial circumstances, age and retirement goals may mean it is time for a change. Aggressive and growth options are high risk, and you may have to sustain significant losses to maximise your return in the long-term. If retirement is a long way off for you, then you have sufficient time to recover from any losses. However, as your income stabilises and your retirement comes closer, consider shifting to balanced options for moderate growth or conservative options, providing a lower return but carrying a lower risk.

Changing a will after death

Contrary to popular belief, a will may be effectively changed after a person's death.

Entering a deed of family arrangement (DFA), also called a deed of variation, is a way to vary the terms of a will. This agreement can be established provided that all interested parties come to a consensus on a particular outcome. A DFA is a viable option in certain circumstances where a consensus can avoid the costly and time-consuming process of litigation in courts.

Doubts about the meaning of the will

There is no guarantee that the deceased person was in a sound state of mind when drafting the will or received legal assistance. By using a DFA, interested parties can amend any uncertainties in a way that is most favourable to them rather than relying on unpredictable judgements from courts.

Redistributing the estate

Beneficiaries may wish to redistribute the estate amongst themselves or may need to change the allocation of assets if new parties are added to the will. Although the specifics of succession law differ amongst the states, an interested party with a close personal relationship with the will maker can apply to contest the will if they are left out. Deliberate exclusions written into the will and long estrangements may not be enough to prevent a claim succeeding. The court will weigh up financial circumstances, disabilities, age and the nature of the relationship to reach a decision. If the claim by the interested party is likely to succeed, a DFA will amend the will with greater resource efficiency than the courts.

Block a challenge to the will

If an interested party not listed as a beneficiary seeks to challenge the will, a DFA may come in handy. The deed can be used as a means of compromising a claim against the estate agent where there is a challenge to the will. However, this rule differs in states like Queensland and Victoria where parties cannot contract out of their rights to bring a family provision claim.

Create an estate proceeds trust

An estate proceeds trust (EPT) allows the movement of assets between beneficiaries to occur in the most tax effective way. Keep in mind that under current tax legislation a person receiving property via a will from a deceased individual has three years from the death of the deceased to transfer the property to the EPT.

Eligibility and document checklist:

Legal advice would be helpful prior to drafting a DFA. Once the decision is made, follow this checklist to ensure your document is binding and complies with taxation legislation.

- All interested parties, beneficiaries and the executor should sign the deed to demonstrate the mutual consent of all involved.
- In certain states, the court may approve the document, providing certainty.
- No adverse Capital Gains Tax consequences will be incurred if requirements of section 128-20(1)(d)(i) of the Income Tax Assessment Act 1997 are met.
- Applying for eligible concessions minimises any Stamp Duty triggered by the agreement.

Buying the right shares

Your portfolio's profitability comes down to buying the right shares at the right time.

Conduct relevant research and avoid common blunders made by investors, so your next move in the share market is the right one.

Research the company

Before you invest, you should research a range of companies. If you want a low-risk investment with a reliable return, consider a blue chip company listed in the ASX50. Look into speculative companies that are not in the ASX100 if a high risk, high performance investment is right for you.

Key questions you should ask in your research of companies, particularly those offering high-risk, high return shares, should include:

- Is the company growing?
- Is the company in debt and if so how much?
- Will the company's goods and services be in demand long term?
- What is the rate of growth and is it slowing?
- Does the company's management have a good track record?
- Is the industry stable, seasonal or unreliable?

Know your economy

Gaining an understanding of the current economic environment is vital in assessing whether shares are likely to accrue profit or incur losses. Business websites, government sources and news outlets should provide you with information on whether the economy is in a growth or recession period. Look at interest rates, government policy, exchange rates and the global economy to give you the most comprehensive guide.

Avoid common mistakes

Heed these warnings to avoid making a regrettable purchase:

- Avoid hasty investments in shares with one-off profit spikes
- Do not develop an over-reliance on forward-looking statements or predictions
- Do not be tempted by high dividend yields as they may indicate a falling share price