Is super not so super anymore

Why are we talking about this...

- Superannuation reforms
  - Reduction in contribution caps
  - The Abolishment of AntiDetriment
  - $1.6Mn cap
  - Changes to franking credits
- Estate Planning considerations
  - Death Benefits Tax; CGT; Stamp Duty; Business assets
  - Centrelink, ATO, Bankruptcy & Family Law issues
  - Financial, Elder & STD (Sexually Transmitted Debt) issues
  - Blended families
- Estate Administration considerations
  - Personal tax
  - Cost bases
  - The financial acumen of the next generation
  - Estranged families
- Gender evolution & impact on our profession
- What is ‘normal’ these days
- As professionals, can we afford to ‘do nothing’?

Alternative strategy options

What else is available?

Let's consider:

- Investment (Insurance) bonds
- Gearing
- Use of non-super structures

Sue Herrald

National Specialist – Investment Bond

IOOF Holdings

Case Study - TODAY

Bill and Brian are both 45 and have a clear goal to retire when they turn 55.

- Retire pre their preservation age of 60.
- Currently maximising their superannuation contributions caps through employer contributions.
- Need to have the ability to withdraw funds on a monthly basis to give them a regular income stream to fund their lifestyle, from retirement to at least preservation age (60 years old).
- Prefer not to access their superannuation until absolutely necessary.

Let’s set the scene: their current situation

- Earning some $180K pa jointly ($100K pa + $80K pa ea respectively)
  - Have a child (just about to start university)
    - Bill is biological father
  - Brian now looking to earn higher income ($80K -> $100/120K pa)
  - They are almost debt free (approx. $100K remaining, with $400K equity in PPR)
- Super assets of $500K jointly
  - Have been receiving SGC, and have been doing some modest salary sacrifice (5%) of wages
  - Now looking to increase to max caps each ($50K overall)
- Other planning considerations
  - Will still have excess cash pa (some $30K each post tax)
  - They have some $$’s currently sitting in cash ($50K in mortgage offset/redraw)
  - MAY receive an inheritance, but want to exclude from planning so it will be a ‘bonus’
  - Agreed to NOT pay for university fees, but likely to do so anyway
  - Want to retire in 10 years

What to do – Option #1

- As they will be maxxing out their super caps ($25K each), what can they do?
- They want to retire ‘early’, where can they invest?
- Consider an investment (sometimes referred to an insurance) bond
  - Access
  - Tax efficient
  - No ‘loss’ of franking credits
  - No requirement for extra tax work

Consider an Investment Bond

- As they have some $50K sitting in their mortgage, they can use this as 'seed funding' to commence their non-super investment
  - Borrowing to invest -> tax effective debt
- In addition to their mortgage & salary sacrifice commitments, they can also save $5K pm ($60K pa)
- Assuming 5% return (after fees & taxes)
  - Can access
  - Is tax efficient/effective
  - No 'loss' of franking credits
  - No requirement for extra tax work
  - Can be used as collateral (gearing)

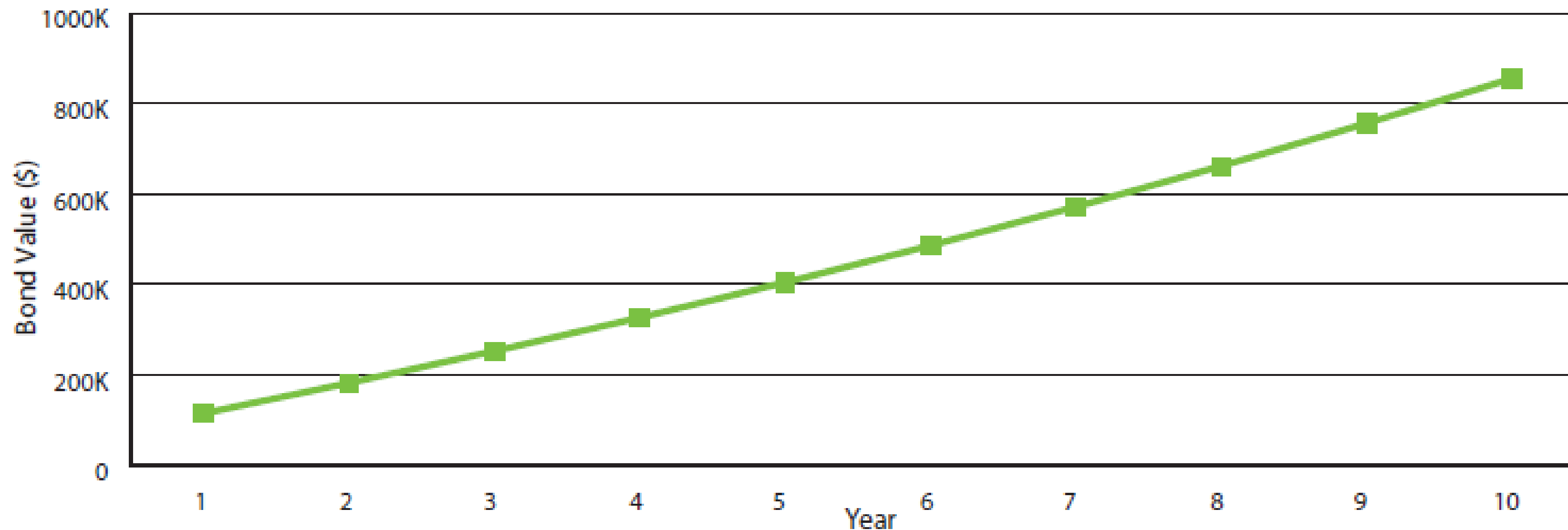
Initial Investment: $50,000
Monthly contributions: $5,000
Net return: 5% (after fees and taxes)[1]

The 10 year period is just a 'line in the sand', an investment bond is accessible anytime and continues until withdrawal.

Years	10
Contributions	$650,000
Growth	$204,756
Value of bond	$854,756
Tax free benefit after 10 years[2]	$854,756

Consider an Investment Bond

- The following graph shows how this might work
- And is not really different to the ‘regular savings plan’ methodology for salary sacrificing into super…



Consider an Investment Bond

- The following table shows the numbers
- In 10 years time, they have some $850K
  - It is ‘tax paid’
  - They can extinguish any/all debt outstanding
  - They can payout any/all HECS/HELP debt
  - They can use this and not touch their super (so it keeps growing)
  - As NON-super, they can also gear as well

Year 1	$0	$110,000	$113,982
Year 2	$113,982	$60,000	$181,162
Year 3	$181,162	$60,000	$251,702
Year 4	$251,702	$60,000	$325,769
Year 5	$325,769	$60,000	$403,539
Year 6	$403,539	$60,000	$485,198
Year 7	$485,198	$60,000	$570,940
Year 8	$570,940	$60,000	$660,968
Year 9	$660,968	$60,000	$755,498
Year 10	$755,498	$60,000	$854,755

Consider Gearing

- Assuming we continue to use the same investment bond, the following table shows the numbers IF we also incorporated gearing
- In 10 years time, they now have some $900K
  - It has been tax effective
  - It is still 'tax paid'
  - They can STILL extinguish any/all debt outstanding (incl payout any/all HECS/HELP debt)
- BUT…
  - Is it worth the risk?
  - Perhaps in other scenarios

Margin Loan Summary	Geared
Total Interest Expense	$77,387
Average LVR over term of investment	24%

Summary of Investment Activities

	Geared Investment					
Year	Investment Value	Loan Balance	Own Equity Contributed	CGT Payable if realised	Net Cash Flows	Net Profit if realised
1	$208,553	$89,000	$115,000	-$459	-$395	$4,158
2	$286,894	$100,000	$175,000	$928	-$442	$10,525
3	$356,322	$100,000	$235,000	$3,316	$705	$18,710
4	$427,832	$100,000	$295,000	$5,560	$3,165	$30,437
5	$501,488	$100,000	$355,000	$8,223	$6,979	$45,244
6	$577,353	$100,000	$415,000	$11,317	$12,188	$63,224
7	$655,494	$100,000	$475,000	$14,855	$18,833	$84,472
8	$735,979	$100,000	$535,000	$18,849	$26,957	$109,087
9	$818,879	$100,000	$595,000	$23,315	$36,604	$137,169
10	$904,266	$100,000	$655,000	$34,063	$47,821	$163,024

Bryan Ashenden

Head of Financial Literacy & Advocacy

BT Advice & Private Wealth

BT FINANCIAL GROUP

Case Study
same family, now 10 years on

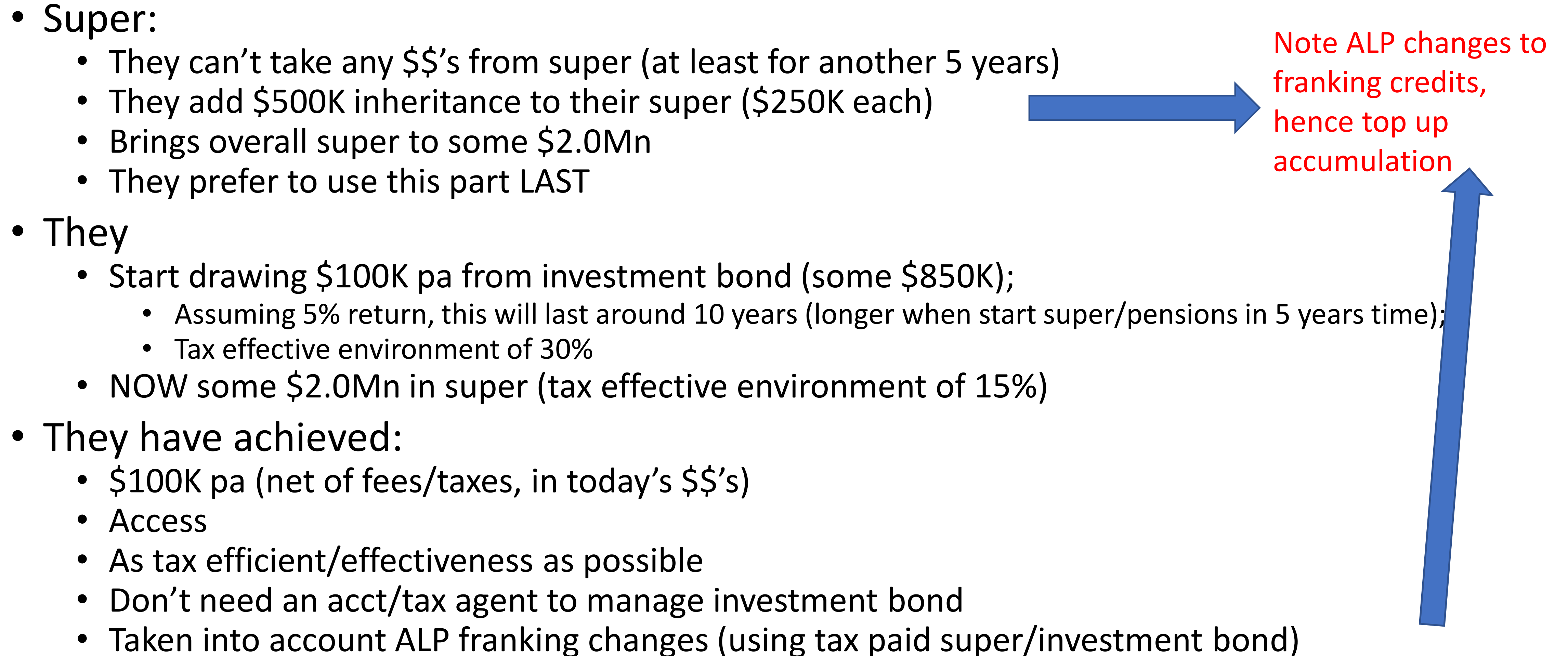
Bill and Brian are NOW both 55 and are about to retire

- Their preservation age is still 60.
- Following your advice, they've been
  - Maximising their super contributions for the last 10 years;
  - Adding to their non-super portfolio (investment bond) for the same time frame;
  - Paid off their debt; and
  - Paid their child's university fees (because they could).
- Now need to have the ability to withdraw funds on a monthly basis to give them a regular income stream to fund their lifestyle:
  - They estimate they need some $2K pw (some $100K pa);
  - This will also take into account regular travel
  - Spoiling their family
- They prefer to use up as much of their non-super $$'s BEFORE they touch their super, which has been earning quite nicely (but they haven't talked to you about this yet)

Case Study
same family, now 10 years on

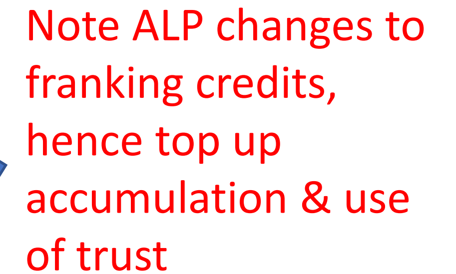
- They are/have:
  - Debt free (paid from regular cashflow);
  - HECS/HELP debt free (paid from regular cashflow);
  - STILL $850K left over in their investment bond; and
  - Some $1.5Mn in super
  - About to receive a small/modest inheritance (approx. $500K)
  - Adult independent child just starting their own family
- They STILL need/want:
  - $100K pa (net of fees/taxes, in today's $$'s)

How – Option #1



How – Option #2

- Super aside (see previous slide), they
  - Redeem 100% Investment Bond in entirety
    - Now, 100% tax paid (no CGT/Tax payable upon redemption)
  - Establish Family Discretionary Trust
    - Invest $$’s through trust
    - Doesn’t form part of estate
    - Can assist family if required
  - Commence drawing down $100K pa
    - Same/similar investments as investment bond;
    - To ensure non-mkt correlated returns, use term annuity to assist with cashflow
- They have achieved:
  - $100K pa (net of fees/taxes, in today’s $$’s)
  - Access to their cash
  - As tax efficient/effectiveness as possible
  - Need to use acct/tax agent to assist manage Family Discretionary Trust
  - Taken into account ALP franking changes (using tax paid super/investment bond)



Other considerations?

- What if Bill and Brian were also running a business together?
  - What would be best way to structure?
  - Small business considerations?
  - Estate planning v asset protection?
- Trust and company considerations
  - Fixed v discretionary trust
  - Control
  - Distributions
  - Estate planning & administration

Peter Burgess

General Manager

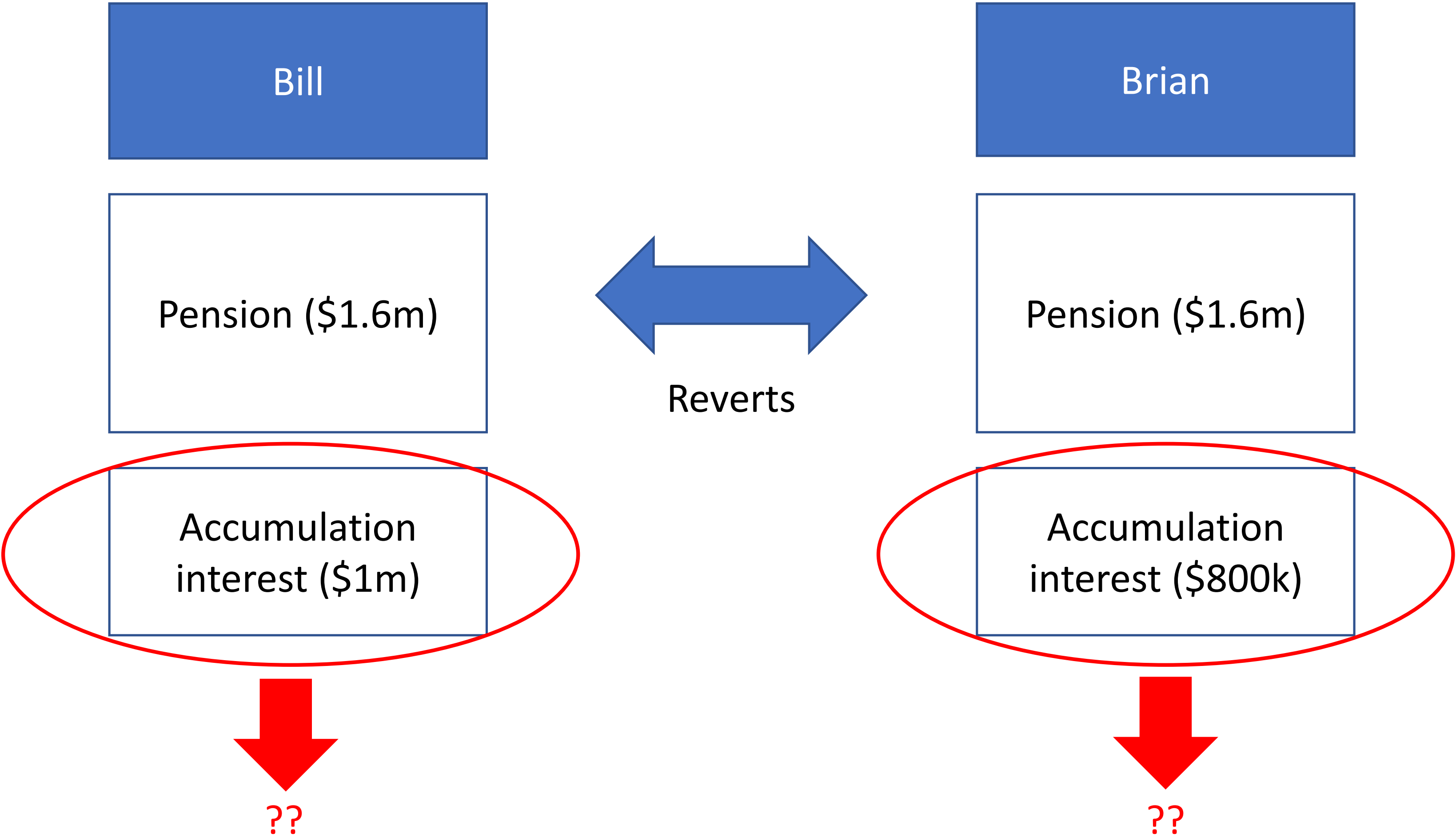
Technical Services & Education

SuperConcepts

Same case study, just fast forwarded another 15 years…

- Bill and Brian now retired and in their mid 70s
- Have used up all the $$'s in their investment bond
- Now have accumulated $$'s in super (SMSF) with combined balances in the fund of $5m
- Only deriving NANE pension income from their SMSF – no other income
- With your advice, their super/pensions have grown:
  - Bill has $1.6m in the pension phase and $1m in the accumulation phase (70% taxable component)
  - Brian has $1.6m in the pension phase and $800k in the accumulation phase (40% taxable component)
- Pensions revert to each other
- Their adult independent child has two children of their own (2 adult grandchildren), BUT none currently engaged in creating or managing the family's wealth but want to build their financial acumen
  - Remember, Bill's biological child, NOT Brian's…
- Concerned about the impact of the super reforms and beneficiaries dwindling their inheritance
- Bill suffered a health scare recently.

Pre/Post reforms



Fund has accumulation interests – paying tax?

Fund balance	Investment earnings	ECPI	Tax payable (pre-reforms)	Tax payable (post-reforms)	Less franking credits	Net tax (pre-reforms)	Net tax (post-reforms)
$5m	$200,000	64%	$0	$12,189	$25,714	($25,714)	($13,526)

Assume 4% investment return

Assume 30% allocation to Australian shares paying fully franked dividends & 4% dividend payment.

If accumulation interests invested in own names?

	Bill ($1m)	Brian ($800k)	SMSF ($3.2m pension)
Taxable income	$45,143	$36,114	$0
Prime tax	$6,218	$3,404	
Medicare	$903	$136	
Less: SAPTO	$622	$1,751	
Less: LITO	$323	$445	
Less: LAMITO	$444	$200	
Tax due	$5,732	$1,144	$0
Less franking credit offset	$5,143	$1,114 $4,114	$0 $16,457
Net tax payable	$589	$0 ($2,970)	$0 ($16,457)
Capital gains			
Capital gain after 5 years*	$160k	$127k	
Capital gains tax#	$13,057	$8,377	$0

*Assume capital growth of 5%p.a. #Assume 80% CGT assets.

Halving the discount for individuals

ALP

If left in SMSF = ($13,526) $0

Total = ($18,838) $589

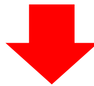
Total = $21,434

If left in SMSF = $22,935

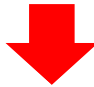
Option #1:
What about using a
Discretionary Family Trust NOW?

NOTE: ALP – 30% tax on Distributions to mature beneficiaries

Bill & Brian's combined ***accumulation*** interests ($1.8m)



Discretionary (Family) trust



Assume $72k distributable income (4%)

Bill ($14,400)	Sue ($14,400)	Adult child ($14,400)	Adult GC1 ($14,400)	Adult GC2 ($14,400)

Death benefit tax?

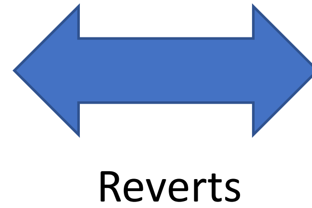
	Tax on death*
Pension	$190k
Accumulation	$119k
	$309k

*If paid to a non-tax dependant @17%

Bill

Pension ($1.6m, 70% taxable)

Accumulation interest ($1m, 70% taxable)



Reverts

Brian

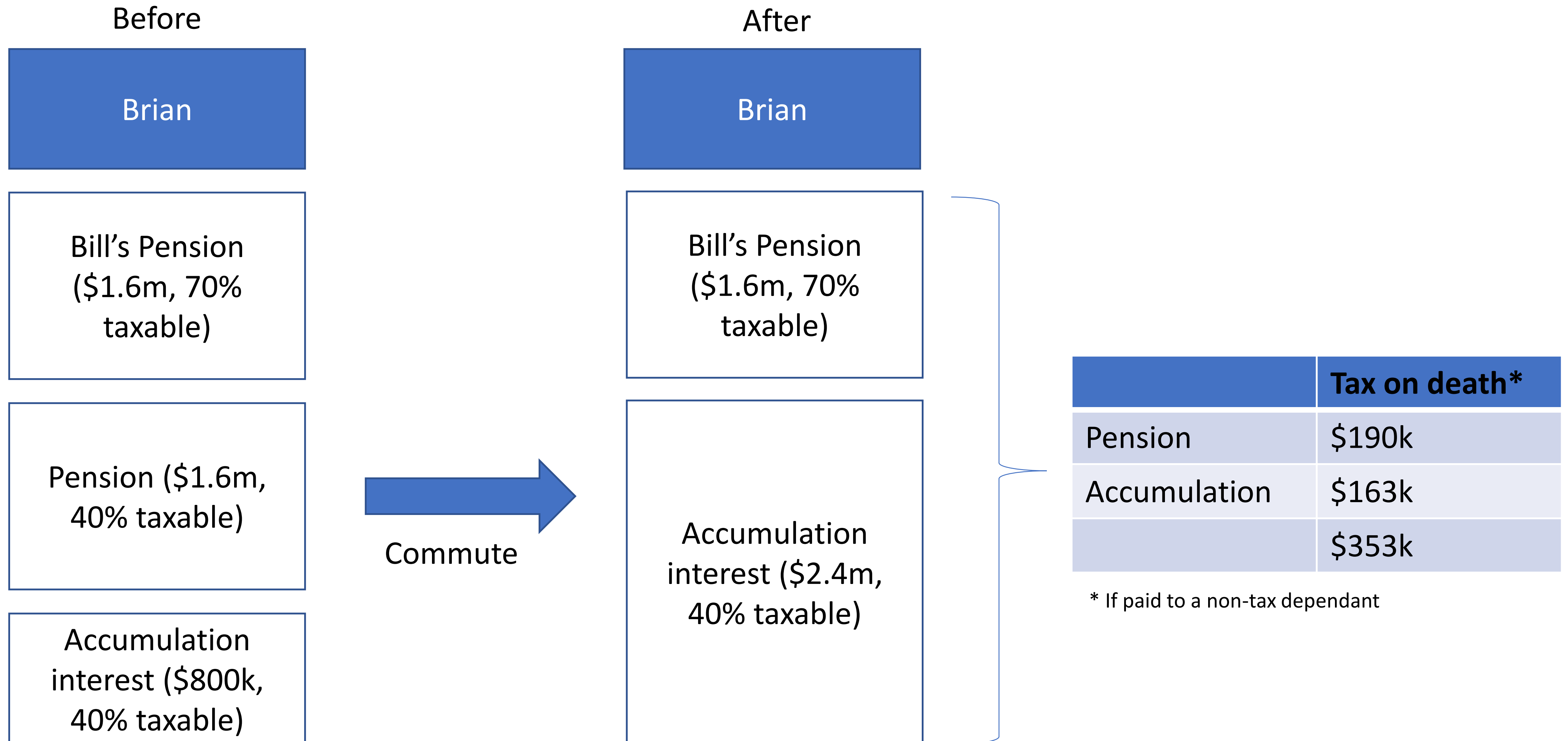
Pension ($1.6m, 40% taxable)

Accumulation interest ($800k, 40% taxable)

	Tax on death*
Pension	$109k
Accumulation	$54k
	$163k

*If paid to a non-tax dependant @17%

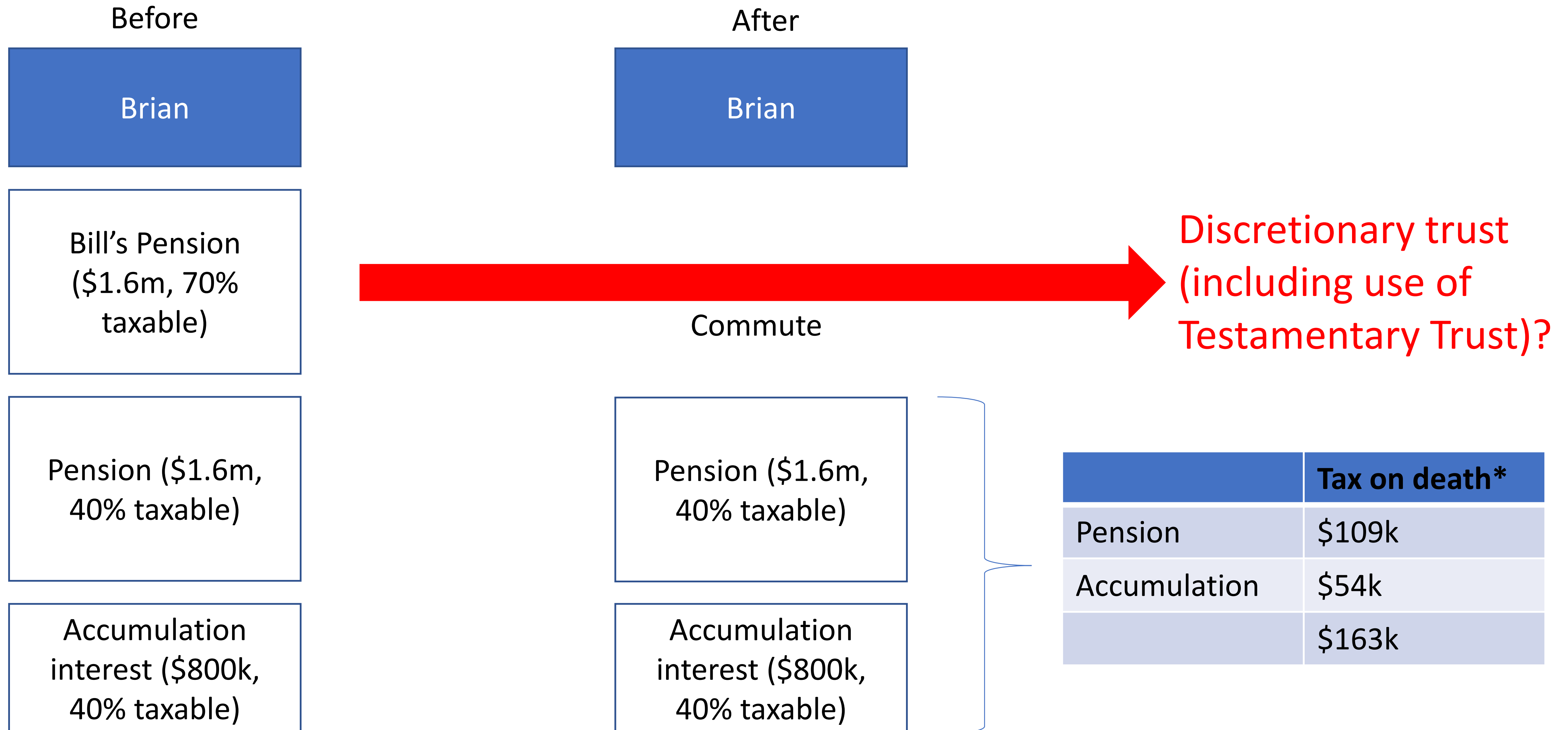
Option #2: Bill passes away (no change)



	Tax on death*
Pension	$190k
Accumulation	$163k
	$353k

* If paid to a non-tax dependant

Option #3: Bill passes away (uses a TT)



	Tax on death*
Pension	$109k
Accumulation	$54k
	$163k

Panel discussion

Conclusion

- Super is no longer the panacea
  - There ARE other options available – as FP professionals, the responsibility rests with us to either upskill & specialise, refresh our knowledge, or refer to a specialist
- Can we use other strategies (and who offer these product solutions)?
  - Do we have the skill set? Do we have the accreditation? Does our licensee/PI allow us to advise in this area?
- Other considerations…
  - Strengthen relationships with Accountants, Lawyers, Mortgage Brokers, etc
  - Centrelink, Family Law, Bankruptcy, Other Jurisdictions
  - Financial & Elder Abuse
  - Estate Planning just became even more complex than it already is
    - Recent case studies aside, are the executors and/or the EPOA ready? Are you?
  - Estate Administration is now a growing ‘business’
    - Are we up to speed (no pun intended)
  - Governmental and legislative volatility
  - Economic volatility and sequencing risk

Questions??