



# Financially Speaking



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## Super Sting



### Did you realise that some unfortunate super fund members face a 93 percent tax rate on certain superannuation contributions?

This breathtaking rate is triggered when fund members exceed the annual caps on both concessional and non-concessional contributions.

Contributions that exceed the cap on concessional contributions count towards the cap on non-concessional contributions – and could push a member's non-concessional contributions over the limit.

Here's how that hefty tax figure is calculated:

- Contributions that overshoot the concessional cap are taxed at 31.5 percent, in addition to the 15 percent standard contributions tax – bringing the tax take, so far, to 46.5 percent.
- Contributions that overshoot the non-concessional cap are taxed at 46.5 percent, bringing the possible tax total to 93 percent.

Excess contributions are, of course, highly topical at this time with many taxpayers now completing their 2009-10 tax returns, the Government's halving of the cap on concessional contributions from 2009-10, and with the tax office's recent updating of its online information regarding excess contributions.<sup>1</sup>

The tax office can, in "special circumstances", disregard excess contributions or reallocate them to another financial year. But the ATO warns: "It isn't enough that your circumstances were unusual for you."

And the ATO explains that unintentionally exceeding the caps, misunderstanding the law or facts, or being given incorrect information does not "amount to special circumstances on their own".

Particularly as the amounts involved in excess contributions tax are potentially so large, it is important to speak with your financial planner when planning your super contributions.

**Source: Robin Bowerman, Head of Retail, Vanguard Investments Australia**

<sup>1</sup> <http://www.ato.gov.au/individuals/content.asp?doc=/content/00119316.htm>



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# Should I choose a fixed or variable loan?

**Even though interest rates have started to climb, we are still experiencing a market with historically low interest rates and given this, many clients regularly ask us if they should switch their variable rate loan to a fixed rate. Every client's situation is different, so it is important to seek advice when making decisions about the type of loan that best suits your needs.**

Mostly the questions are generated by the media hype surrounding rates but it is important to remember at these times that it's just that, "Hype". Bad news sells and the media is very quick to publicise concerns and focus on the negative.

Media reports should all be taken with a grain of salt. Last time interest rates started moving up, the media predicted interest rates would get up to 15%. Many people at the time quickly fixed their interest rates and ended up being stuck at rates around the 8.25% mark. The problem is the rates only got as high as 8.75% and shortly thereafter reduced back to

5.25%. All those stuck still at 8.25% are no doubt wishing they had instead waited.

That being said, there is still no guarantee as to what this rising interest rate market will do, and while we may listen to the media we should not take it as Gospel either. The motto of the story here is that the media, and in fact often even the "Experts" can get it wrong.

If you are considering fixing the interest rate on your mortgage it is important to think about a few of the following differences between a fixed and a variable interest rate loan:

## **Fixed:**

- Limitations on making extra repayments - usually limited to about \$5,000 - \$10,000 per annum
- No redraw facilities available
- Higher exit fees for early termination of the loan
- Rate fixed for between 1 – 5 years

## **Variable:**

- Extra payments can be made to reduce your Interest cost

- Redraw facilities are available
- No extra penalties above the standard ones for early termination of the loan
- Your payments can be adjusted to match the movements in interest rates

Keep these points in mind before deciding to fix your interest rate and at the end of the day make sure the loan features will suit you.

For more information about fixed versus variable rates, or to discuss your current or future home loan requirements, speak with your financial planner.

## **Source: Lonsdale Finance Choice**

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# What is Investment Risk?

All investments have some form of risk associated with them i.e. they all expose you to the chance you could lose money (either notionally or permanently). This article discusses seven of the more common types of investment risk.

### The risk of permanent loss of capital

Poor quality investments usually experience falls in their value from which they never recover. In extreme cases, their value can fall to zero.

### The risk of volatility

Investment volatility is the risk of the value of your investment moving up and down. With high quality investments, their values should move up more than they go down.

Investments which are expected to produce higher long term returns (such as shares) tend to experience higher levels of short term volatility.

On the other hand, investments which are expected to generate lower long term returns (such as bonds) usually experience less volatility in the short term.

This can be seen in the charts to follow which show the range of historical returns for various asset classes over various periods, as well as their long term average returns.

As you can see, the longer you hold your investments the less they are affected by volatility. For example, the range of returns for Australian shares in any single year has been -42.6% to 58.2%. However, the range for 10 year periods has been 3.5% to 14.6% p.a.

**Note:** Investors who redeem their investments after a fall in value turn a notional loss into a permanent loss.

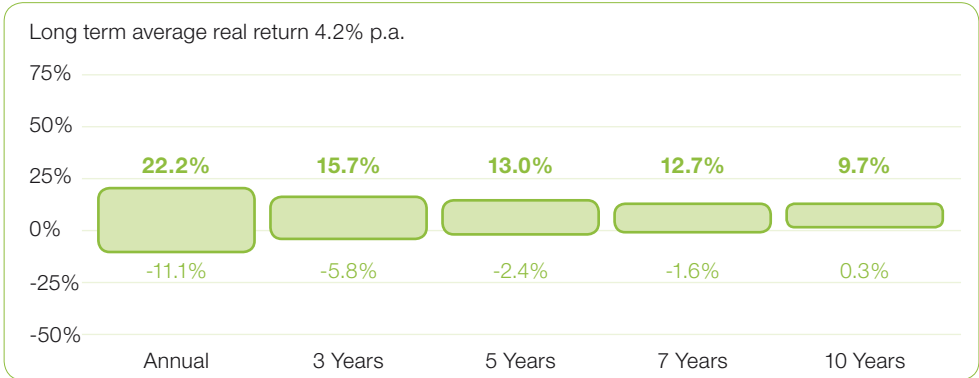
If they are high quality investments, this is usually a poor decision, because high quality investments should recover from falls in value.

### Wealth risk

This is where your investments do not generate sufficient returns to help you achieve your wealth or retirement objectives. This is typically the case when a person chooses not to employ an asset allocation which has a higher level of investment volatility (and also a potentially higher return). In that case, the person will need to lower their wealth or retirement expectations.

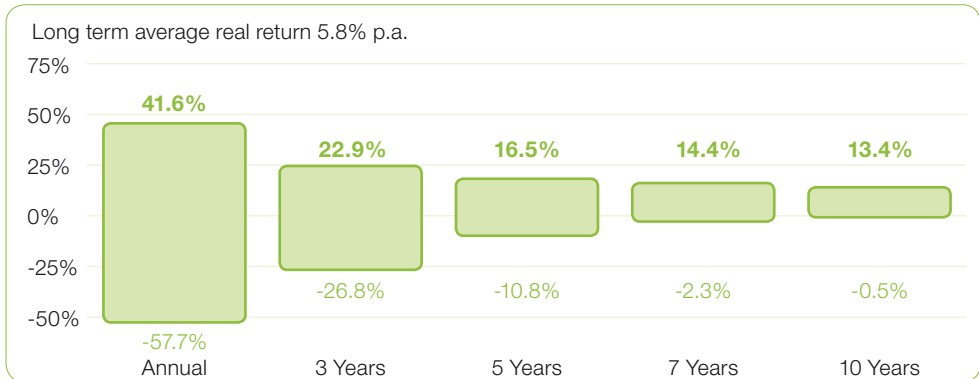


## Range of Returns (after inflation) – Australian Bonds



**Source:** Australian Unity Personal Financial Services. These figures are based on returns for 1975 to 2010 for the RBA Fixed Interest Index. Inflation average 5.4% p.a.

## Range of Returns (after inflation) – Australian Listed Property



**Source:** Australian Unity Personal Financial Services. These figures are based on returns for 1975 to 2010 for the ASX Listed Property Trust Accumulation Index. Inflation average 5.4% p.a.

## Credit risk

Credit risk usually applies to fixed term investments and means that the institution you have invested with may not be able to make the required interest payments or repay your money.

## Inflation risk

This is where your money loses purchasing power because your investments do not keep pace with inflation. Cash is one investment which usually falls prey to inflation risk.

## Liquidity risk

Investments which are fixed term expose you to liquidity risk. For example, if you need to access your money from fixed term investments before the term expires, you may be prevented from doing so under the contract. Or, if you can access your money, it might take longer than you want, and/or you may be charged significant penalty fees.

Poor quality share and property investments also expose you to liquidity risk. The risk is that no one will want to buy them from you or will only buy them at a substantial discount.

## Currency risk

When you invest overseas, your money is usually converted to the currency of the country in which you invest.

If the Australian dollar subsequently rises in value compared to the other country's currency, your investment will be worth less to you. On the other hand, if our dollar falls in value, your investment will be worth more.

How can you manage investment risk?

Investment risk can be managed using three prudent principles of investing:

- Only invest in high quality investments
- Construct a properly diversified portfolio
- Regularly review your investments to ensure they continue to maintain their quality.

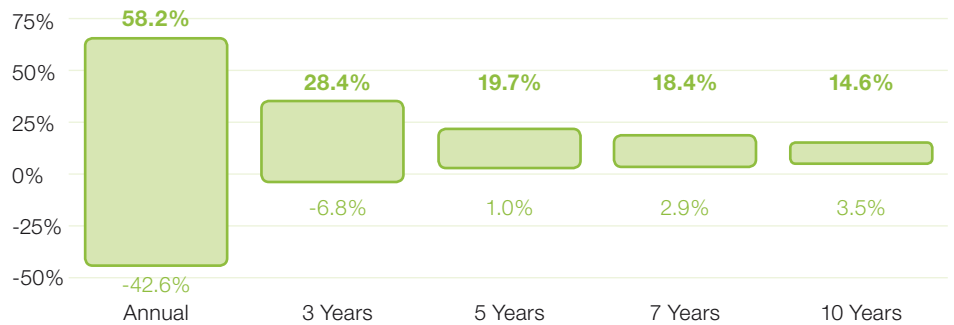
Always speak with your financial planner when making decisions regarding your investments.

### Source: Australian Unity

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## Range of Returns (after inflation) – Australian Shares

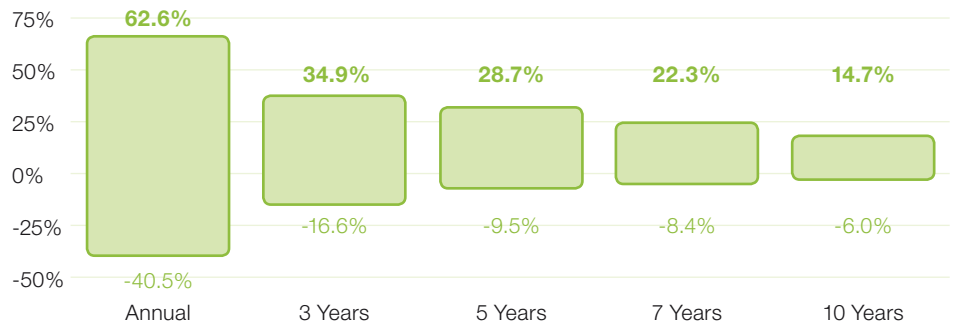
Long term average real return 9.0% p.a.



Source: Australian Unity Personal Financial Services. These figures are based on returns for 1975 to 2010, for the ASX All Ordinaries Accumulation Index. Inflation average 5.4% p.a.

## Range of Returns (after inflation) – International Shares

Long term average real return 6.3% p.a.



Source: Australian Unity Personal Financial Services. These figures are based on returns for 1975 to 2010 for the MSCI Accumulation Index. Inflation average 5.4% p.a.

# Starting a family

**There are a lot of uncertainties involved in starting a family – from choosing the right nappy strategy through to working out the best approach for disciplining your little bundle of joy.**

Starting a family also has its own unique set of financial implications that you're likely to encounter for the first time. Here are our tips for financial health while you're starting your own family.

## A new budget

Now that you're planning for the birth of a child, take some time out amongst the preparations to consider your finances. Take a look at your budget and adjust it to take into account:

- the amount of time you and your partner will be away from work. If you're employed, your employer may grant you paid maternity and paternity leave, and many mothers are entitled to twelve months unpaid leave after having a baby. Consider how time off work

will affect your family income and adjust your budget accordingly.

- medical costs associated with childbirth. Your health insurer and medical practitioners will be able to indicate the extent of these costs.
- any additional health insurance cover you may require.
- general costs associated with raising a child, such as clothing, nursery items, prams and so on.

Budgeting for these costs will help you to manage your income and expenses during the early years of starting your family.

## Government benefits

Depending on your circumstances, you may be entitled to Government assistance in the form of one or more of the following benefits:

- Maternity Payment (previously the Baby Bonus and Maternity Allowance).
- The Family Tax Benefit – an ongoing payment to assist with child rearing costs and to assist single parent families.

- Child Care Benefit – an ongoing payment to assist with your child care costs.
- Maternity Immunisation Allowance – a one off payment for your child's immunisation.
- Large Family Supplement – for families with three or more children.
- Multiple Birth Allowance – assistance for those having a multiple birth involving at least three children.
- Rent Assistance – ongoing rental assistance for lower income earning families.
- Health Care Cards – access to concessions on medical expenses.
- Double Orphan Pension – assistance in caring for a child who is an orphan.

Your eligibility for these benefits will depend on a number of factors such as your income level, your residence status in Australia and the age of your children.

### Family assistance

If you're unsure of your eligibility for any of the Government's family assistance schemes, speak with your financial adviser or accountant, visit [www.familyassist.gov.au](http://www.familyassist.gov.au) or phone the Government's Family Assistance line (**13 61 50** from 8am – 8pm Monday to Friday or **13 12 02** for information in languages other than English).

### Taxation advice

Now that you're in the family way, reconsider your tax and income arrangements. There are some tax concessions specifically available to parents, such as the Child Care tax rebate that covers a portion of your out of pocket child care expenses for approved child care. (Out of pocket expenses are child care fees not already covered by the Australian Government's Child Care Benefit). Speak to your financial adviser to ensure that your family is minimising tax wherever possible.

### Deciding whether or not to go back to work

Obviously, you will have personal factors to consider when deciding whether or not you should return to work. It is important that you consider your current financial situation and your plans for the future.

The significant costs of modern day child care will also come into play if you're not one of the lucky few to have full time family members available to care for your kids. Incorporate a realistic estimate of child care costs into your budget and assess whether the personal and financial incentives for returning to work justify the costs of child care.



### Your child's financial future

As a responsible parent, you may have already considered securing your children's financial future by starting a regular savings or investment program. Speak to a financial adviser for advice on the best savings and investment program for your family. They will consider the economic environment, your financial situation, your goals and the level of investment risk you're willing to take to come up with a financial plan best suited for your family's needs. As those needs change, your financial adviser will also be able to adapt the plan to your changing circumstances.

Another vital step in securing your children's financial future is to take some time to create a Will and inform your family and friends of your wishes for your children and your assets should the worst happen. You should be able to bind your superannuation provider to distribute your superannuation according to your wishes if you make a 'binding nomination'.

When considering insurance, remember that obtaining insurance, such as life, disablement and salary continuance insurance, through your superannuation account can be a very tax-effective and efficient way to ensure you and your family's financial future.

### More children

With all of these steps in place, there's nothing to stop you from having many more children, right? Whatever your family plans, we wish you and your new family the best of luck.

Always speak with your financial planner when making decisions about your financial future.

**Source: Zurich Investments Australia**



# 7 things to think about before withdrawing from your fund

**Given the recent volatility in sharemarkets, you may be thinking about withdrawing your money from your fund. But before you do, it's important to evaluate the consequences.**

Whether you are thinking about transferring your money to another investment, paying off some debts or buying something else, it's important to consider the consequences of withdrawing or redeeming your investment.

Here are seven things to consider before withdrawing money from your managed fund investments.

## 1. The fund's objectives and timeframe

Each managed fund has an investment objective and suggested timeframe for investment. If you have been invested for a shorter period than the suggested timeframe and withdraw, the objective of the fund may not be achieved as there hasn't been enough time for the fund to ride out any short term volatility.

Choosing to remain invested in a fund with a long term timeframe through periods of

volatility increases the chances of the fund achieving its objectives.

Investing for the long term, rather than trying to make short term changes, gives you the best chance of reaching your financial goals.

## 2. The effect on your whole portfolio

If your managed fund investment is part of a longer term strategy, withdrawing now could mean it may take even longer for you to achieve your financial goals.

For example, if you are invested in an Australian share fund and decide to move these funds into cash, you may be sacrificing higher returns over the long term.

Moving your money into another investment may even increase the risk within your overall portfolio, due to a change in the level of diversification.

## 3. There will be tax implications

When you withdraw from a managed fund after it has gone down in value, you end up crystallising your loss.

This means you lose the potential for your investment to go up in value, as well as taking on that capital loss for tax purposes.

## 4. Time, not timing

While many investors try to 'time' their investments into strongly performing assets, knowing the right time to buy and sell requires as much good luck as good judgement.

Factors such as interest rates, exchange rates, commodity prices and consumer spending all come into play to influence the performance of investment markets.

Figure 1 – Timing the market since December 1989

Market	Fully invested return % pa	Missed 10 best months % pa	Missed 20 best months % pa
International shares (S&P 500)	8.21	3.64	0.25
Australian shares (ASX All Ordinaries)	9.91	5.87	2.67

Source: IRESS. As at 31 December 2009.

Figure 1 (opposite page) shows the returns of international shares and Australian shares, and what would happen if investors who tried to time the market were not invested during the 10 best months and 20 best months since 1989.

It shows that investors would have received significantly lower returns if they missed the best 10 months, and an even more significant reduction if they missed the best 20 months.

Investing for the long term, rather than trying to make short term changes, gives you the best chance of reaching your financial goals. So when markets are fluctuating and you feel like withdrawing your investment, ask yourself whether the peace of mind is worth missing the upside when markets recover.

### 5. The grass is not always greener

While moving out of one managed fund into another may work in the short term, not all funds perform well year in, year out.

If fact, moving to a better performing fund could leave you worse off than you were before.

If you crystallise a loss, you will also be moving less money than you originally had, making it even harder for your money to go up in value.

### 6. Be aware of the fees to withdraw

Each fund and fund manager may charge different fees to withdraw some or all of your investment. The fees associated with withdrawing from one fund and then investing into another will impact your overall return.

It's important that you check with your fund manager or read the latest product disclosure statement to find out the total cost of moving your money.

### 7. Discuss your situation with a financial adviser

You should always talk to your financial adviser before making any decision about your investments. They can help you understand what's happened with your investment and how it fits in with your long term investment strategy.

#### Source: Perpetual Investment Management

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# Women lacking on insurance protection

**When it comes to having enough insurance cover in place, there should be no 'it can't happen to me' attitude.**

That's because accidents and illnesses do not discriminate, so whether you're male or female, single or married, it's equally as important to have adequate insurance in place to protect you from unforeseen events.

As logical as all that sounds, there are still many women who are very underinsured when it comes to cover for their life or a critical illness.

### Getting total cover is important

While many women may take the time to shop around for health, car or home and contents insurance, important protection such as life insurance or critical illness covers are often not considered or put on the back burner.

What this means is that if they were to die suddenly, their family would receive no pay out to cover things such as funeral expenses, outstanding debts, or to make up for the total loss of their income. In the case of a total and permanent disability, which prevented them from working, or a major critical illness, there would be no funds

available to pay for long term hospital or health care.

Without cover, some women won't be able to afford a medical specialist if they are unwell and may have to wait for treatment.

### Are you single?

The Australian Bureau of Statistics has calculated that a fifth of Australia's population now live alone. Many are single women who have large debts and mortgages.

Getting divorced, becoming widowed, or looking after adult children is getting more common for many Australian women. But many women fail to protect themselves for unforeseen illnesses if no-one is around to take care of them.

Those women who do think of life insurance usually insure their husband or partner before themselves. While this is important, more women are recognising that if they are unwell they may need money for a carer, a housekeeper, or just some money to maintain a reasonable living standard. Being unwell can be tough for your family. It can be even worse for women with children or who are on their own.



## A sobering health check

Becoming critically ill is not rare. One in four women will be diagnosed with cancer of some sort in Australia, according to the Australian Bureau of Statistics.

By taking out life insurance, women can insure themselves for a fixed monthly income or lump sum payment if they become critically ill.

The amount of cover needed depends on various factors, such as age, income and debt levels.

Critical illness life insurance can pay a lump sum amount or a fixed monthly amount if a specified critical illness is suffered.

Increased awareness about cancer, screening programs and early detection means that cancer is being increasingly diagnosed in women at an earlier stage so can be more effectively treated. These types of early abnormalities are known as 'pre-invasive cancers'.

If left untreated, there is an increased risk that a mass of abnormal cells or tumour is formed and spreads to different parts of the body. These are known as malignant tumours, commonly referred to as cancer or invasive cancer, and can really bring home the potential need for life insurance for critical illness given the cost of treatment.

Your financial planner can help you find the right types of cover for your needs and to set your cover at the most appropriate level.

Source: MLC / AVIVA

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# The importance of regular reviews

**Regular reviews of your financial plan are the stepping stones to optimising your financial security.**

### Dealing with changes

The financial world is always changing. Political, economic, legislative and social factors will continue to change long into the future. Ongoing reviews with a professional financial planner who understands and monitors these changes will assist in supervising and tailoring your financial schedule.

### Case study

Charlotte and Craig were married for two years before they consulted a professional financial planner. With a baby on the way, the couple needed advice on budgeting and Craig's investments. Although it was suggested they be involved in an ongoing review service, Charlotte and Craig declined. They believed the advice offered would set them up for life.

Five years later their family had grown and Charlotte had permanently left the workforce. They also inherited money and gained equity in their home. In short, their circumstances had changed drastically and their plan no longer reflected this.

Had Charlotte and Craig been involved in the review process, their financial planner would have been able to offer them a report on Craig's investments, a tracking of his portfolio as well as any further advice they had needed.

'Nobody plans to fail but many fail to plan'.

An ongoing review service would likely include annual meetings to review your long term financial position. A financial adviser should listen to your needs and goals and tailor their service to help meet them. You can enjoy life today, knowing that your future is in expert hands.

Source: Lonsdale Financial Group



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