INVESTMENT SOLUTIONS

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WHAT'S INSIDE

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GOING THE DISTANCE

THERE WAS A TIME WHEN TURNING 100 WAS WORTHY OF A NEWS STORY. BUT PROJECTIONS ARE THAT BY 2050, THERE WILL BE ENOUGH 100-YEAR OLDS IN AUSTRALIA TO ALMOST FILL THE OLYMPIC STADIUM IN SYDNEY. THAT'S 78,000 CENTENARIANS TO BE PRECISE.

Have we cracked the code for immortality? Probably not. But the fact remains that many of us will live a lot longer than our grandparents did.

Today, the average life expectancy for Australian men is 79[1], and for women 84. But once people actually reach age 65, their life expectancy rises to 86 and 89 respectively[2].

When you consider the average Australian still intends to retire at around age 63, that's more than 20 years out of the workforce. This brings with it some new challenges from a financial planning perspective.

1. BALANCING YOUR WORK LIFE

Working longer has the obvious benefit of helping you save more for retirement. But employment also offers valuable social and mental stimulation — benefits that many people miss out on in retirement.

These days, working for longer doesn't have to mean slogging away at the same job for another 10 or 20 years. Growing numbers of baby boomers are already exploring new options like setting up consultancies, pursuing a new career altogether, or taking more flexible work hours to help look after grandchildren.

One of the benefits of a Transition to Retirement (TTR) strategy is that it allows you to take a pay cut to do something different — while using income from your super to maintain your current lifestyle.

While doing this means you are drawing on your retirement savings sooner, having that extra balance in your life could potentially help prolong your working life by a number of years.

2. KEEPING YOURSELF FIT AND ACTIVE

Advances in medicine, improved diets and greater awareness of the need to stay active even in old age mean that today's 65-year olds are often in extremely good shape. So retirement offers a lot more than it used to.

Plans of travel, lunches with friends and outings with the grandkids, need to be factored into a retirement budget. Likewise, your expenditure on gym memberships, physiotherapy and chiropractic care may increase — which may mean it's worth hanging onto your health insurance.

Having greater spending needs also reinforces the value of investing in growth assets like shares and property, even in retirement. One of the benefits of having a longer investment horizon is that market downturns can become more of a blip on your portfolio radar, rather than forcing a major belt-tightening.

3. MAKING YOUR SAVINGS LAST

Not only are we living longer, baby boomers will continue to comprise a growing segment of Australia's population. This has seen a raft of new products become available that are pitched specifically at helping retirees maintain a comfortable lifestyle for longer, including reverse mortgages, annuities that address longevity risk and account-based pensions.

Getting the right balance of spending and saving is critical for retirees, and you always need to factor in the need for additional capital in later retirement — particularly when you consider the costs associated with aged care (which can run into the hundreds of thousands of dollars).

The ability to keep your money in the super environment indefinitely, may help in this regard. And there are capital preservation strategies available that allow you to accumulate for your later retirement tax-effectively, even after you've retired.

4. IS YOUR RETIREMENT PLAN ON TRACK?

Given the nature and complexity of retirement solutions and strategies, retirement planning is best undertaken with the help of someone who understands the latest rules and regulations.

WHO WANTS TO BE A CENTENARIAN?

Year	Number of people aged 100+
2008	3,000
2030[3] (projected)	12,000
2050[4] (projected)	78,000

1_ Australian Life Tables 2005-07. Australian Government Actuary, Commonwealth of Australia, 2009.

2_Australia's Longevity Tsunami — What Should We Do? Actuaries Institute White Paper — August 2012.

3_Medical Journal of Australia, The changing face of the Australian population: growth in Centenarians, Robyn L Richmond, MJA 2008; 188 (12): 720-723.

4_Department of Health and Ageing, Record Number of Australians Living to be more than 100 Years of Age and New Phenomenon of "Super-Centenarians".

MARKET UPDATE

GLOBAL OVERVIEW

While there's been a certain level of improvement in the second half of 2012, overall the financial markets have struggled to find a solid and consistent footing through 2012.

The mixed messaging from European politicians in regard to the ongoing management of the European debt crisis, together with ongoing concerns about weaker global growth (in both developed and emerging market economies) continues to impact investor confidence.

More broadly, the debt crisis is showing no signs of easing, with the Euro-area government debt increasing to 88.2% of GDP in the first quarter from 87.2% in the previous three months of 2011. This is the highest level since the euro was introduced in 1999. At 132% of GDP, Greece has the highest debt burden, while Italy's debt remains at 123% of GDP. It's the key reason as to why countries such as Spain and Italy need to reduce their funding costs, as both the level of debt is impeding the ability for the countries to focus on other more growth opportunities.

In the US while the economy continues to expand, the pace of growth has slowed in recent months, with GDP growth now below 2%. More recently, the Federal Reserve Chairman Ben Bernanke testified to Congress on the state of the US economy, noting that the slowdown is impeding the ability for a meaningful reduction in the unemployment rate.

The other issue facing the US economy is the impending 'fiscal cliff' where US lawmakers must reach agreement on setting a budget for 2013. Failure to do so will result in a number of 'automatic stabilises' kicking into gear, resulting in the expiry of a number of the tax concessions and other fiscal support measures that have assisted in providing support to the economy. A failure to reach an agreement on the budget for 2013 in a timely manner has the potential to push the US economy into recession.

In Europe, consumer and business confidence has been made worse with at least 5 of the 17 member bloc countries currently in recession and the euro area jobless rate that currently stands at 11.4%. Also, the region's largest economy in Germany is beginning to show signs of slowing, further impeding the growth outlook.

Across Asia the picture remains very similar. The most recent data suggest that industrial and manufacturing activity is still struggling. In China alone, manufacturing has declined for the 11th straight month in September. Equally Japan is also struggling with recent industrial production figures below market expectations. Weaker Japanese growth has seen the bank of Japan (BoJ) expand its asset purchase program in recent periods as a means of providing additional monetary stimulus.

In Australia, while the Australian economy continues to track relatively well to its global peers, there is an increasingly likelihood that the next quarter will be more challenging for economic growth. While the RBA has maintained a steady course on interest rates more recently, we continue to expect that rates will fall further from current levels (3.25%). This should provide some buffer to parts of the economy impacted by the high Australian dollar, with the potential for lower interest rates to also assist in the improvement of business and consumer confidence.

Piers Bolger
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Advice & Private Banks

PROTECTING YOUR PAYOUT

DO YOU KNOW WHAT WOULD HAPPEN TO THE PAYOUT FROM YOUR SUPER OR PENSION ACCOUNT IF YOU PASSED AWAY? YOU MIGHT BE SURPRISED TO HEAR THE ANSWER.

One day, when you pass away at the ripe old age of 110, it would be nice to think that anything you leave behind would magically make its way to the people you loved, and the charities you wished to support.

Because that's generally a pipedream, most people prepare a Will to set down their goals and wishes.

But what about the assets you hold inside superannuation? Do you know with certainty how they would be treated if you're not around?

While there was a time when people would cash out their super lump sums when they retired, these days most people are keeping their money in account-based pensions to maximise the tax-effectiveness of their retirement income.

However, what a lot of people don't realise is that the beneficiary they nominate to receive their super, or the balance of their account-based pension, actually overrides their Will.

This means even an up-to-date Will may not be enough to ensure your wishes are carried out.

HOW DO BENEFICIARIES IN SUPER WORK?

When you open up a super account, you generally nominate who will receive your super benefit in the event of your death. This can be done through either:

- A binding death benefit nomination
  The Trustee is "bound" to pay the benefits to those nominated.
- A non-binding death benefit nomination
  The Trustee can use its discretion, and usually pays the death benefit to a dependant or a legal personal representative.
- An automatic reversionary beneficiary (account-based pensions only)
  The Trustee continues to pay the pension income the account-holder would have received to their nominated beneficiary.
- Maximising your benefits
  A crucial element of estate planning is ensuring you're passing the right assets to the right beneficiaries from a tax perspective.

While most superannuation benefits are made up of tax-free and taxed components, an untaxed component can arise where insurance proceeds form part of the benefit, or the benefit is paid from a public sector scheme.

In situations where there are multiple beneficiaries, it's often advisable to divide assets in a way that optimises tax treatment (see case study).

If someone has a super balance and an investment property, it may make sense to pass on the super to a dependant — like a spouse or a child under 18 — and pass the investment property onto an adult child who's not considered a dependant.

KEEPING IT IN THE RIGHT HANDS

While the tax-effective distribution of your assets is a worthwhile goal, first and foremost it is about ensuring your assets end up in the right hands.

For advice specific to you and your family, it's important you talk to your financial adviser.

CASE STUDY

Garry married Silvia five years ago. It was Garry's second marriage, and he had two adult children from his previous marriage.

In Garry's Will, he specified that he wanted all of his assets split evenly between Silvia and his two children. However, Garry had nominated Silvia as the binding beneficiary of his superannuation.

Garry's Financial Planner pointed out that if Garry passed away today, all of his super would be paid to Silvia, not his estate.

Garry's Financial Planner recommended he keep Silvia as the beneficiary of his super, as she would be able to receive those benefits tax-free as his spouse. He also suggested Garry amend his Will to include an 'equalisation clause' so that the superannuation proceeds are taken into account when determining each beneficiary's entitlement.

Davis suggests people work with their Financial Advisers and solicitors to ensure everyone has a clear understanding of the implications of both their Will and beneficiary nominations.

If there's any complexity in your life — like if you're in a second marriage, or if you have multiple beneficiaries — estate planning is a vital part of your financial plan.

INSURANCE IN THE SPOTLIGHT FOR SMSFs

UNDER NEW REGULATIONS, TRUSTEES OF SELF MANAGED SUPER FUNDS (SMSFS) NOW HAVE TO CONSIDER LIFE INSURANCE AS PART OF THEIR INVESTMENT STRATEGY. HERE'S WHAT THAT MEANS FOR YOU IF YOU HAVE AN SMSF.

To encourage more SMSF Trustees to take up life insurance, new regulations were introduced in August this year — meaning that Trustees must now consider insurance as part of an SMSF's investment strategy.

For new SMSFs, this will mean that Trustees must consider whether it is appropriate to hold insurance for members, at the time the fund is established. For existing SMSFs, this obligation arises when the investment strategy is next reviewed — which is now required to be done on a 'regular' basis.

The level of life insurance ownership within SMSFs remains extremely low — less than 13% according to the 2010 Super System Review[1].

In light of this change, it is important for Trustees of SMSFs to understand the benefits of holding insurance inside the SMSF beyond the considerations for members of providing for dependants.

Holding life or permanent disablement cover over a member (or all members) of the SMSF may provide the liquidity often necessary to allow an SMSF to pay a death or disability benefit in cash. This can be particularly useful if there are 'lumpy' assets in the SMSF, like property, that the Trustees wish to retain in the fund.

WHAT TYPES OF INSURANCES ARE AVAILABLE IN SUPER?

There are three types of insurance commonly held in SMSFs:

- Life insurance — which pays a benefit on the death of a member.
- Total and Permanent Disability insurance — which pays a lump sum on the permanent disability of a member.
- Income protection — which pays a regular income payment if a member is unable to work temporarily.

WHY HOLD LIFE INSURANCE IN SUPER?

Under the new rules, Trustees are only required to "consider" life insurance, not actually purchase it. However, using your SMSF to hold insurance may have significant advantages.

One of the main benefits is that you can pay your insurance premiums using superannuation money. And as the case study below shows, this means you may be able to pay for cover using before-tax income.

CHOOSING A STRATEGY THAT'S RIGHT FOR YOU

The effectiveness of life insurance inside super depends on a number of factors, including:

- the type of insurance purchased
- your marginal tax rate
- your ability to contribute within the relevant contributions caps, and
- your personal circumstances.

CASE STUDY

Chris recently had his insurance needs assessed and determined the level of Life and Total and Permanent Disability (TPD) cover required. The annual premium for the required cover is $5,000.

If Chris holds the policy in his own name, he must pay the premium from his take-home pay. Chris is on the top marginal tax rate of 46.5%, so he needs to earn $9,346 before tax to pay a $5,000 premium.

However, when Life and certain TPD insurance policies are held within super, the premiums are tax-deductible to the fund. This tax deduction can be used to offset the tax payable on salary sacrifice contributions.

As a result, Chris only needs to salary sacrifice $5,000 of his pre-tax income into his SMSF to pay the premium. That's a saving of $4,346 compared to holding the insurance outside of super.

In the event of an insurance claim, the proceeds of the policy would be paid to Chris' super account. As such, Chris needs to consider the tax payable (if any) on proceeds withdrawn from super when determining the ownership structure of his insurance.

1_'Super System Review Final Report' — Super System Review Panel, June 2010

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