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Summer 2007 Newsletter

'Chris' comments'

Australia's Superannuation Tax Haven

Australia's Superannuation Tax Haven

Why not put ALL your money into super

With the Simpler super reforms the obvious strategy for everyone over the age of 55 is to have all their assets and investments (except personal use assets like a home or car) in a superannuation fund. However the government is not foolish, after all if everyone put everything into super and didn't pay tax withdrawals after age 60, tax revenue would dry up. Can you imagine a wealthy sixty year old member of a super fund contributing \$20M into a fund and then drawing upon as needed? The tax savings would be more than \$1M per year!

To stop the abuse of the tax free status of super, the government has introduced strict limits on how much can be contributed into a super fund on behalf of a member. Those limits and when they apply are as follows:

- Where the contribution has been deductible (now known as a concessional contribution) the limit is \$50,000 each year or \$100,000 if you are over 50 in the year when the contribution was made. However the over 50 rule ceases on June 30th 2012. The concessional contribution limit applies from the 1st of July 2007 with current aged based limits applying for the 2006-2007 income years.

- Where the contribution is a non-deductible (now known as a non concessional contribution) the limit is \$150,000 each year or \$450,000. Like the concessional contribution rules, the limit on non-concessional contributions commences on 1st July 2007.

- From 1st of July 2007 golden handshakes and other retiring allowances will be taxed in the hands of the employee and cannot be transferred into superannuation. For those persons at or beyond preservation age the first \$140,000 is taxed at a concessional rate of 15% with the remainder at the top marginal tax rate. For those employees below the preservation age the first \$140,000 is taxed at 30 % rate with the top marginal tax rate to apply thereafter. These are transitional rules for employment contracts entered into pre 10th may 2006 where a payment is made prior to 1st of July 2012.

Where do self managed super funds (SMSF's) fit in?

There is \$1 trillion of investments in superannuation. SMSF's where the members of the fund control the fund, have been a big hit over the last ten years. From nowhere in 1994, by 1st of October 2007, there was 400,000 SMSF's with \$218 billion in assets. According to the ATO the average size of a SMSF is more than \$660,000 in assets. Independent research by the Australian Stock Exchange has shown that members choose SMSF's for four major reasons.

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- **Control**— All members of the fund must be trustees of the fund or directors of the funds company trustee. In those positions the members have full control of the fund—when benefits can be paid, what to invest in, insurance for members and so on. For many who have come from a business background and are happy to take responsibility of their superannuation, the SMSF is the vehicle of choice.
- **Choice**— The trustees of a SMSF are provided with a wide range powers and investment choices under the SMSF Strategies trust deed. Investments can range from equities to residential property, instalment warrants, agriculture, property development and the list goes on.
- **Taxation**—SMSF are a great vehicle for many over 60's to set themselves up with tax free lifestyle income for the rest of their lives as well as passing assets to the next generation with little or no tax. In addition, the trustee of the SMSF pays a low rate of 15% tax on investment income unless the investments are being used to pay an income stream, where no tax is paid on income or capital gains. As well the trustee of the fund can use imputation credits to reduce tax payable on the fund.
- Family SMSF's are essentially family super funds allowing four members of a family to house their superannuation investments into a common low taxed vehicle where they have choice and control.

Chris has just passed his SMSF qualification and is now available to talk to you if you are looking at a Self Managed Super Fund. Please call our office on 8431 8222 for more information

From Credit Crunch to Recession ?

When the US sharemarket took a sharp dive last August, following the collapse of some high profile Wall street hedge funds, the global investment community watched on apprehensively. Was the crisis in the American sub-prime mortgage market which had triggered the collapses, serious enough to send the US economy into full blown recession? Or was this as bad as it was going to get ?

In an environment of uncertainty and heightened risk, it looked like a credit crunch was on the cards. US banks stopped lending and liquidity all but dried up overnight. Things were looking decidedly dire when some swift footwork from the US Federal Reserve Bank managed to quell market nerves, but not before it injected billions of dollars into the financial system to encourage inter bank lending) and slashed the official interest rate by 50 basis points.

Global equity markets rebounded strongly, touching new highs, but could it be that they were premature in assuming the worst was now over ? And why should Australian investors still be concerned by the state of the US housing market?

Currently the US comprises around 30% of the global economy. In turn, consumer s are the key driver of global economic growth .

The availability of credit has always been vital in shaping US spending patterns, but, in recent years, credit growth has spiralled out of control to the point where household gearing levels are starting to dictate the economic outlook. Fuelled by the real estate boom of the past eight years, US consumption became increasingly dependant on ever-rising house prices and the ability of Americans to continuously refinance their huge mortgages and cash out equity to fund the purchase of plasma screen T. V's, new cars and other consumables.

As a result, US debt has grown from 150% of gross domestic product to (GDP) in 1980 to a whopping 350% today.

As the average American became saturated with debt, the banks turned to less creditworthy customers to lend money to and keep the credit cycle going. These lower quality "sub prime" loans made up 40% of new borrowings in the past two years.

In recent months, mounting defaults on these so called "liar loans" have infected financial markets, given they were securitised into high grade, mortgage backed securities and loaded into collateralised debt obligations (CDO's) The valuations of many of these assets are now in tatters and this proved to be the undoing of some high profile hedge funds. The global economy is now caught in a bind, having relied on US growth for so long to keep the wheels ticking over. The biggest source of that growth—the US consumer— is tapped out and no other economy seems capable of picking up the slack. Even China, long touted as a new growth engine is still less than a quarter of the size of the U.S And Chinese growth hinges on the strength of American consumer demand—so any pronounced US downturn is likely to impact growth in Asia's largest economy. Any weakness in China would impact demand fro Australian resources—and so the domino effect continues.

Despite high hopes that quick action by U.S policy makers may have forestalled disaster, the outlook continues to unravel, it is anticipated that foreclosures could reach one million by year-end. And the outlook does not improve over the next 18 months, with an estimated two million adjustable rate mortgages due to be reset, placing further mortgages in jeopardy of foreclosure.

Article from Zurich



Sorrento Victoria

It's Not All Doom and Gloom

Rates

I'm sure by now that we have all heard the news that Mortgage holders can expect further interest rate increases in 2008.

As discussed in the Spring Newsletter (please contact Money Works if you would like a copy of the Spring edition) there is continued pressure on the global credit markets due to the sub prime crisis in the US and because of this there has been a brief "wait and see" attitude in Australia. However, according to Westpac chief economist Bill Evans, the strong Australian economic outlook means that the reserve Bank will need to lift interest rates by a possible 0.5% within the first half of 2008.

Home loan affordability

Australian families required 33.8% of family income to pay an average home loan in September 2007, the worst result for 25 years aside from an 18 month period from March 1989 to September 1990. Amongst OECD countries, only the Netherlands and New Zealand have a higher percentage of mortgage debt as a percentage of household disposable income, with the level of debt in the Netherlands being promoted by a policy of negative gearing for owner-occupied homes.

On the positive side

According to the Real Estate Institute of Australia house prices and other dwellings generally continue to increase over most of the country, with Adelaide seeing a 2.3% increase in the September quarter.

During 2006, house prices rose across Australia, ranging from 0.6% in Sydney to 38.7% in Perth.

Current evidence suggests that Sydney and Adelaide prices have remained moderate in 2007. Even moderate growth in Melbourne, Brisbane, Canberra and Hobart during 2006 has already begun to show in all cities except Hobart, and it has been seen that price growth in these cities have remained that way throughout 2007.

Perth and Darwin had an outstanding year for median house price growth in 2006, 2007 although there is evidence that the boom times of 2006 are slowing in Perth.

However, net overseas migration to Western Australia is high, and the unemployment rate is low (3.1%), which will assist in maintaining stronger demand than in other parts of the country. Darwin continues to have strong prospects for price growth into 2007, 2008 in response to the commodities boom and high demand for quality cotemporary property.

The Rental Market

The demand for rental properties is outstripping supply in every capital

city in Australia, with a weighted Australian average vacancy rate of 1.7%, well below their industry vacancy rate benchmark of 3.0%. This is not likely to improve in the short term, based on falls in investor financing, and housing affordability.

In Conclusion

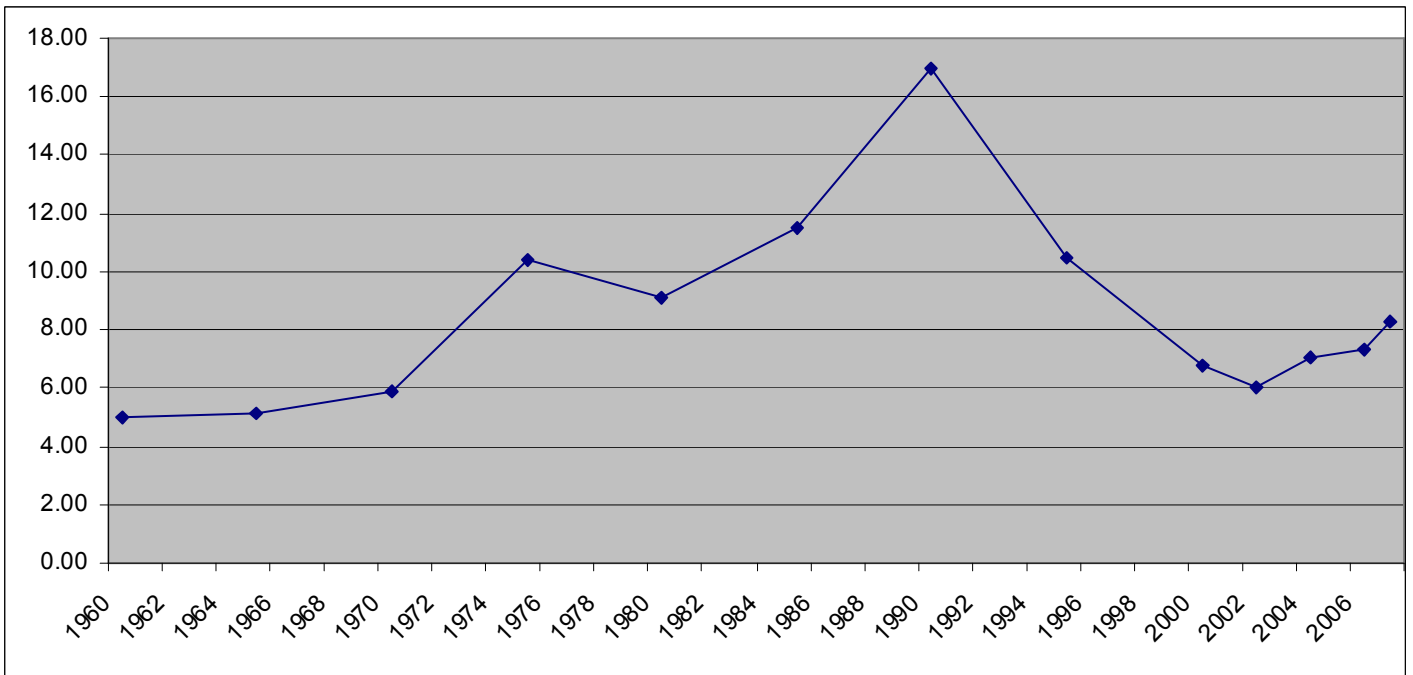
Owning property in the current market can be a positive or stressful experience. If the Mortgage you currently have is causing concern, have it reviewed to ensure that you are not paying too much. I would be happy to meet with anyone who would like a "Mortgage Check".

Article sources include The bureau of Statistics, Real Estate Institute of Australia

Vicki Harris
Mortgage Relief



0408 820 443



Interest Rates Over time

Source REA

Is your estate plan current?

Estate plans drafted before the advent of the Simpler Super System should be reviewed to ensure that the strategies are still valid and/or maximize the benefit under the new rules .

Under the Simpler Super system introduced last July, lump sum death benefits from super no longer incur tax, regardless of the balance, provided the funds are paid to a death benefits dependent (as defined under tax law). A death benefits dependant is a spouse, former spouse, child under 18 or someone else in an interdependent relationship with the member at the time of his or her death.

Meanwhile, an income stream can now only be paid to a member's dependent as defined under super legislation. This includes a child who at the time of the member's death is:

- Younger than 18
- Disabled and any age
- 18–25 and financially dependent on the member.

Moreover, an income stream to a member's child (excluding a disabled child) is only payable to until he/she turns 25 at which point any residual capital is paid as a tax free lump sum. Where an adult child has been included as a beneficiary in a binding death benefit nomination but he/she isn't eligible to receive an income stream under the new legislation, the fund rules will determine how the benefit is to be paid; either at the trustee's discretion or to the deceased's estate.

If your estate plan was drafted before the introduction of the Simpler Super System, it's important to revisit your strategies to ensure they're not only still viable under the new system but also make the most of new opportunities.

Two important Estate planning considerations that need to be taken in to account include how the proceeds will be taxed and where applicable, whether the payment would be better taken as an income stream or lump sum.

For example, whereas super paid as a lump sum to a death benefit's dependent is always tax-free, the ages of the member and beneficiary can affect the tax treatment of an income stream. If both the member and beneficiary are younger than 60, the inherited income stream will include a tax free portion and a taxable component (see table) The income stream becomes tax free once the beneficiary turns 60.

In turn, where the death benefit will be paid as a lump sum to a non-dependant, such as an adult child, various strategies can be used to minimise

tax payable on the amount, including a re-contribution strategy that boosts the tax free component of the individual's super balance.

Article from Zurich

Taxation of pension payments due to death of a member (Taxed)	Age of beneficiary upon reversion of income stream	Taxation of income taxed (scheme)
60 or older	60 or older	Tax-free
60 or older	Under 60	Tax-free
Under 60	60 or older	Tax-Free
Under 60	Under 60	Tax-free component is tax free. Taxable component is taxed at the beneficiary's marginal tax rate and receives 15% tax offset. Taxable component becomes tax free when beneficiary turns 60

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To make a time with Chris Harris to discuss any of the topics further please call our office on

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Need Help with a Home Loan? Contact Vicki Harris at Mortgage Relief on 0408 820 443



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