keeping an eye on finance

focus

Issue: Autumn 2007

Welcome to the latest edition of Focus

In the last Federal budget, the Howard Government unveiled a series of major proposals designed to make superannuation a more attractive investment vehicle for all Australians.

Many of those changes come into effect on 1 July 2007 this year, and in this issue we take a snapshot of the key amendments to assess what they mean and how they will impact workers saving for retirement.

Importantly, some of the changes that take effect from the start of the next financial year mean there is a narrow window of opportunity at the moment to transfer assets with a large value held outside of superannuation into a concessionally taxed environment if action is taken before 30 June 2007. This may involve the selling of shares and/or other investment assets.

This opportunity relates to a fundamental change, whereby pension payments from a superannuation income stream will become tax free once an individual reaches age 60. This is in addition to the existing tax free earnings environment that a superannuation income stream enjoys. So for those nearing retirement, this may be a once-off opportunity to potentially avoid a much larger tax liability in the future.

Also in this issue we take a look at geared investments, that is the use of borrowed funds to invest in assets such as property or listed securities. With both the share market and the property market showing strong growth, the use of products such as margin loans can be an attractive option for investors wanting to build a long-term investment portfolio.

'Gearing up for long term growth' examines the potential benefits, as well as the potential risks. So, as always, it's important to seek qualified financial advice to ensure that a strategy can be devised that matches your individual circumstances.

Why 2007 is a super year

Australian superannuation is undergoing massive change, and changes coming into effect on 1 July 2007 are expected to create a massive inflow of funds into super funds over the next few months.

These impending changes, introduced in the Federal budget in May last year, are intended to simplify the superannuation system and make the process of saving for retirement more tax effective and easier than ever before.

For many Australians, the changes present an opportunity for life in retirement to be much more comfortable as a consequence of generous tax breaks and other incentives.

in this issue

Words of Wisdom

I never think of the future – it comes soon enough

Albert Einstein

Australian National Consulting Pty Ltd

ACN: 072 563 574
Level 2, 431 St Kilda Road
Melbourne VIC 3004
Ph: 1300 880 789
Fax: 03 9821 4137
www.ancadvisers.com.au

Australian National Consulting

Why 2007 is a super year cont.

Tax free super benefits

Among the major changes, the end benefits tax on superannuation benefits paid as a lump sum or income stream from a taxed fund, will be abolished from 1 July 2007, for all Australians from age 60.

This means zero tax will be payable on any superannuation pension income or lump sums after age 60. With the removal of reasonable benefit limits, death benefit lump sums will also be tax free to tax dependants.

This is in addition to the zero tax paid on earnings in a superannuation pension.

Reasonable Benefit Limits

The existing limit on how much can accumulate within the superannuation environment before being taxed at a higher rate, known as the Reasonable Benefit Limit (RBL), will be abolished from 1 July 2007. This will enable accumulation of an unlimited amount of retirement savings without tax penalty. The RBL had restricted concessionally taxed super benefits to $648,946 for a lump sum and approximately $1.3 million for those who took at least 50 per cent of their super as a complying income stream.

Contributions

People with assets outside of super can make up to $1 million in after tax contributions until and including 30 June 2007 this year. For some, this one off opportunity may be a time to sell the family home to 'downsize' into a smaller dwelling and deposit the remaining funds into super to earn tax-free income. For others with substantial investments, consideration should be given to bringing forward the disposal of these assets if they wish to maximise their superannuation savings.

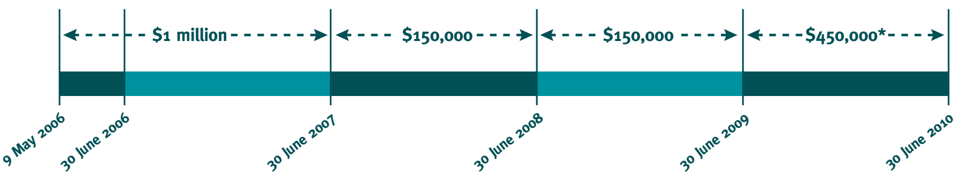
From 1 July 2007 individuals can make up to $150,000 contribution from after tax amounts (known as Undeducted Contributions) into super in any one year, allowing transfers of share portfolios or proceeds from a property or business sale. To accommodate larger contributions, people under age 65 will be allowed to bring forward two years of contributions. This will enable up to $450,000 to be contributed in one year, with contributions in the next two years restricted. However, the $450,000 limit only applies if the annual $150,000 limit is breached.

Self employed

Superannuation contributions by the self-employed are now 100% tax deductible until age 75. Previously, a deduction was only claimable up to age 70, and the amount of deduction was also limited.

Aged based limits

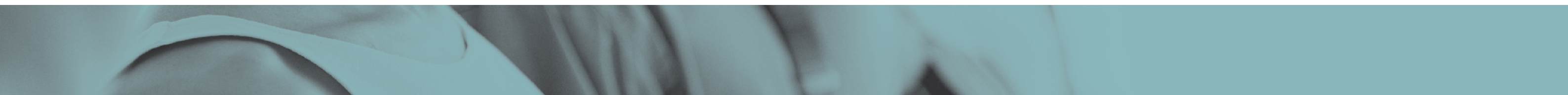
The age-based limits on deductible contributions will



This time line shows the maximum post-tax contributions you can contribute yearly over the next four years

Note: the $150,000 limit may increase due to indexation, but only by increments of $5,000

* By bringing forward the limits on two years of contributions, a person can contribute $450,000 in one year



be replaced from 1 July 2007 with a flat $50,000 per person, per annum. The age to which deductible contributions can be made will also be extended to age 75. This means employees over age 70 can salary sacrifice their wages.

There are also transitional rules which will enable those over age 50 to contribute up to $100,000 of deductible contributions until 30 June 2012. This gives those over age 50 an opportunity to boost their super.

Tax deductions for contributions

AGE	2006/07 limit	2007/08 onwards*
<35 yrs	$15,260	$50,000
35 to 49 yrs	$42,385	$50,000
50 to 75 yrs	$105,113	$100,000 to 1/7/2012 $50,000 from 1/7/2012

Assets test

The Centrelink pension assets test taper rate will be halved from 20 September 2007 so that age pension recipients only lose $1.50 per fortnight (rather than $3) for every $1,000 of assets above the relevant threshold.

Contact us

To maximise your opportunities and take advantage of this super opportunity before 1 July 2007, it's important you act now and contact us. Your overall strategy will require forward planning and budgeting, so we'll need to review your situation and determine whether an opportunity exists for you.

Gearing up for long term growth

Low interest rates, a robust share market, rising property prices and low rental vacancy rates have made for a robust climate for investing.

Yet most of us do not have large amounts of funds readily available to take advantage of the investment opportunities in the marketplace. That's where a high quality borrowing facility can come into play.

Borrowing for greater leverage

A margin loan enables you to borrow funds to invest in different assets other than direct property, such as equities and managed funds. The funds you borrow are generally secured by the underlying investments.

A well-managed strategy, using borrowings to invest for the longer term, can greatly increase investment earnings and accelerate the value of your portfolio over time. However you should be aware that borrowing to invest can also amplify investment losses.

Adding borrowed money to your own funds means you have a larger amount of money working for you.

Fast Facts

From July 1, total taxable contributions ('concessional contributions') made by or on behalf of a person will be limited by a concessional contributions cap. Excess amounts above this cap will be taxed at the highest marginal tax rate by imposing a 31.5% tax rate on top of the 15% contribution tax.

Higher income earners should therefore consider reviewing their salary sacrificing arrangements to ensure they do not exceed the contributions cap.

Gearing up for long term growth cont.

How do margin loans work?

Margin loans offer flexibility and may allow you to borrow more at a later date should another investment opportunity arise or if your portfolio value has increased above your preferred minimum gearing level. Increasing your overall investment power by adding borrowed funds means you may be able to achieve your financial goals sooner. That's because the borrowed funds allow you to multiply the power of your capital and potentially increase your investment returns.

Getting a tax break

With a margin loan you can generally claim tax deductions for interest loan payments. Pre June 30 is a good time to discuss whether you can or should pre-pay interest, up to 12 months in advance, to maximise your tax deductions in the current financial year.

Interest and margin calls

Borrowing to invest can be a very rewarding strategy, however there are always some risks involved.

Firstly, taking out a loan means there are repayment obligations, so it's important to assess your financial capacity to make ongoing repayments. In addition, having a margin loan facility means you could be required to meet what is known as a 'margin call'. A margin call is when the market value of your investment falls below an agreed level, and this may come into play if you use your funds to invest in shares and the market suddenly falls sharply.

A margin call can be met in several ways, such as increasing the level of assets securing your loan, because the underlying value of the secured assets has fallen below the amount owing.

Ask your financial adviser

It's important to seek professional financial advice from a licensed adviser, who can assess your individual circumstances and advise you on the best strategy.

You should seek advice on how much you can comfortably borrow to invest, any tax implications, the types of loan facilities available, and the circumstances in which a margin call may be made under your loan agreement.

Margin lending

Key benefits	Key risks
• more money invested	• potential for margin calls
• achieve greater investment diversification	• losses magnified if asset price falls
• potential higher returns	• rising interest rates
• interest payments are tax deductible	• loan repayment obligations

Fast Facts

From July 1, the treatment of an employer termination payment will depend on whether the payment is considered an 'Employer Termination Payment' (ETP) or 'Transitional Employer Termination Payment' (TETP).

The tax free and taxable component of an ETP must be cashed out from July 2007. There will be no option to rollover to a superannuation fund.

An employee receiving a TETP will continue to have the option of rolling the tax free and taxable component to a superannuation fund, either in part or in full.

Fast Facts

From 1 July 2007, superannuation interests will be comprised of two components:

- tax free component
- taxable component

For people aged 60 or over, all lump sum super benefits paid to a member or paid as a lump sum death benefit to a tax dependant will be tax free when paid from a taxed superannuation fund.

For persons under age 60, the taxable component of a lump sum super benefit may still be taxable.

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