ISSUE 54

WEALTH MATTERS

Your personal guide to wealth creation

INSIDE:

- Costs of investing in property
- Winding up your SMSF
- Binding Financial Agreement Pros and Cons
- And more

How you can stay updated with the investment market

Investing isn't just about whether you have enough money, it's also about researching the market to find the opportunities right for you.

However, due to the availability of information, it is difficult to know where to begin your research. Researching the following areas will give you an overarching understanding of the market and help you identify potentially valuable investment opportunities.

Economic updates

The overall state of the economy will be relevant to most investment opportunities. When the economy is stable, the chances of the company performing well are higher. Accordingly, if the country is experiencing economic decline, it may be more difficult to maintain stability or improve value. Therefore, stay updated with overall economic trends and avoid investing during periods of decline.

Industry Updates

Different industries thrive during different times. If an industry is performing particularly well, invest in companies from that area. There may be exceptional circumstances when companies may thrive despite their industry performing poorly, you will be able to identify these with more experience.

Stock market updates

There are many resources available which keep you updated with the stock market. Depending on the website, you'll be able to gain information about changes in stocks anywhere from 24 hours to 20 minutes after an event occurs. The more often you read these initially, the better you'll get at distinguishing relevant and irrelevant information.

Company updates

Once you are picked a company, ask the following questions before you invest:

- Is the company making more net income than the previous year?
- Are the sales higher than the previous year?
- Has the company been releasing new products and services?

You can often find the answers to these questions either from media sources, or annual reports uploaded by the company on their website. By asking these questions, you will understand how the company is performing irrespective of the state of the economy.

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Costs of investing in property

There are many fees associated with investing in property that impact overall cost and profit.

Costs to buy and sell

Buying and selling property involves multiple fees and costs:

- Stamp duty
- Conveyancing fees
- Legal costs
- Search fees
- Pest and building reports

Should you choose to sell your property, you will also incur agent's fees, advertising costs, and legal fees. You will also be required to pay capital gains tax if your property has increased in value.

Borrowing money to buy

Individuals will often borrow money to invest in property and will need to pay a mortgage. Relying on rental income to cover mortgage isn't ideal as there may be times when the property has no renters.

Costs of owning an investment property

Investment properties don't just come with buying and selling costs, there are also ongoing fees to pay:

- Council and water rates
- Building insurance
- Landlord insurance
- Body corporate fees
- Land tax
- Property management fees (if you use an agent)
- Repairs and maintenance costs

You may be able to claim tax deductions on certain expenses, but you will still have to pay them upfront. If your investment is positively geared then you might be required to pay tax on the rental income you acquire.

In the enthusiasm of investing in property, it can be easy to overlook these costs and fees. However, recognising the short term and long term costs associated with buying and selling property will make navigating your investment much easier.

What is the 'right' amount of life insurance

How do you decide what amount of life insurance is the 'right' amount, especially when there are so many unknowns?

Life insurance should ideally help cover your funeral expenses, pay off mortgages and assist with managing day-to-day expenses:

Debt

Various types of debts such as a mortgage, student loans, car loans, etc. should be taken into account when setting up your life insurance policy. For example, if you have a mortgage of $300,000 and student loans of $25,000, then your policy should cover at least $325,000. But don't forget about interests and extra charges that may apply. Your policy should be a little higher than these debts to account for those additional costs.

Income replacement

Income replacement is especially important if you are the sole income earner of a household. You will need a policy which takes into account your income and then a bit more to account for inflation over the years. The recommended minimum amount of life insurance is 10 to 15 times your annual income, although this may be more or less depending on your personal situation. Both individuals in a married couple may need a life insurance policy, regardless of whether both of them work.

The earlier you begin your life insurance policy the cheaper your premium will be. The later you apply, the higher your premiums are, but you will still qualify! Don't start your policy earlier simply because you are concerned about not qualifying later!

Binding Financial Agreement Pros and Cons

A binding financial agreement could be beneficial to partners with many solely owned assets.

A binding financial agreement is similar to a prenuptial agreement. It is a contract between a married or de facto couple that sets out how their finances will be separated if their relationship ends. *The Family Law Act 1975 (Cth)* contains a provision which facilitates this agreement.

This financial agreement can be made before, during and after the marriage or de facto relationship. But for it to be legally binding, both parties must sign it and have acquired legal advice prior to doing so. The legal advisor should inform parties of the advantages and disadvantages of such an agreement and sign a certificate which states that advice was provided to the parties.

The agreement can cover the division of property and finances, financial support, maintenance of one party after the breakdown of the relationship, and any incidental issues.

The most common reason to enter such a financial agreement is to protect assets an individual owned before getting into the relationship. This allows a distinction between personal and jointly owned assets. Such an agreement also allows parties to protect future income that they may receive through inheritances or investments.

Any allocation of debts such as loans or mortgages can also be made under this agreement, preventing shared liability for a personally owned asset. A comprehensive agreement will reduce costly court proceedings by minimising conflict if the relationship fails.

It may be difficult to discuss such an agreement, especially at the start of a marital or de facto relationship but it is ideal for partners who prefer to keep ownership and responsibilities of their assets separated.

Winding up your SMSF

Towards retirement, individuals may consider switching from their self-managed super fund (SMSF) to a different type of super fund.

There are 2 key reasons why an SMSF fund may not be ideal towards and during retirement:

- SMSF funds are time-consuming and require the trustee to regularly stay updated with the market and implement any changes to investment themselves. For some, this may be stress-inducing and contrary to the relaxation they desire during retirement.
- SMSF funds have ongoing costs which do not apply to other types of super funds. Although these may be affordable when one is working, they may no longer be feasible during retirement.

You may choose to wind up your SMSF if the above reasons particularly resonate with your circumstances. Remember that once a fund has been wound up, it cannot be reactivated, so this decision is vital.

The first step in winding up your SMSF account is to complete any specific requirements set out in the trust deed pertaining to winding up the fund. You will then need to decide whether you want a payout or for the funds to be transferred to another super fund (you will need to choose and create the super fund account).

Regardless of whether you choose to pay out or transfer to another fund, you will need to leave a sufficient amount of funds in the SMSF to pay final taxes or expenses. Then, appoint an SMSF auditor who can conduct the final audit. You will need to complete and lodge the final SMSF annual returns and details about the wind up to the ATO.

Once you have paid any outstanding tax, settled liabilities and ensured that you have received requested refunds, you are able to close the fund's bank account.

This process can get complicated depending on the relationship between trustees, therefore obtaining expert advice on the best route may be beneficial.

Choosing the right income protection insurance policy

Income protection pays part of your income so that you can focus on getting better rather than trying to make ends meet.

Each company can define partial or total disability differently, and you need to meet these requirements if you are to receive benefits. Check the conditions and ensure that they are sensible and suitable for your necessities. If you do meet these conditions, you can receive up to 85% of your usual income for a specified period. This can be extremely beneficial if you are the sole income earner of a household, own a small business, or are self-employed.

When choosing a policy, you need to consider the following factors.

Policy Type

- Indemnity value policy: Insures you for the amount you are paid i.e. if your pay decreases after you buy the policy then you will recei ve a smaller payment. These policies are cheaper and more useful for individuals who have a steady income.
- Agreed value policy: Alternatively, this type of policy is not affected by your income i.e. you will receive the amount of money that was agreed upon when you signed the policy. These can be a bit more expensive but they are useful if your income changes every year.

Waiting period

This is the period of time you have to wait before you start receiving payments and it can range from fourteen days to two years. The longer the waiting period, the cheaper the policy. Before you agree to a waiting period, consider how many leaves and emergency funds you have which could provide you with some leeway.

Benefit period

You will receive your insurance payments for a specified period but how long that period will last depends on the insurance policy. Commonly, policies offer payments for two to five years or until you are of a certain age (e.g. 65). A longer benefit period results in a more expensive policy but also more protection.

Stepped or level premiums

The premium you choose will have a large impact on how much your premiums cost throughout your policy.

- Stepped premiums: The premium is recalculated at each policy renewal and will usually get higher as you age because the chance of claim also increases with age.
- Level premiums: You will start off with a higher premium but there will not be changes to cost based on your age, rather, will occur more slowly over time.

You should particularly consider a thorough life insurance policy if your work tends to involve more risk as there is greater scope for injury.

Why you should not assess risk yourself

The importance of diversifying your portfolio is constantly reiterated, but how do you determine how to diversify?

Portfolios should have low-risk and high-risk investments. Low-risk investments are bonds, fixed annuities, etc. while high-risk investments are international shares, crypto assets, etc. Depending on the individual and their risk profile, the split of low-risk and high-risk investments will differ.

A risk profile is an evaluation of how willing an individual is to take risks. It is possible for an individual to conduct their own risk assessment, although it may not be ideal.

You will need to ask yourself how much risk you are willing to take, how much risk you are capable of taking, and how long you plan to invest. However, answering these questions isn't as simple as looking at your bank account and picking a number you feel comfortable with.

To gauge a better understanding of your risk profile, these 3 main questions can be extrapolated into more in-depth questions. Progressively, answering such questions is no longer as obvious or straightforward. There are ways to calculate the answers to these questions through algorithmic calculations, but even then, you may not be able to weigh and compare one question to another. How do you distinguish the importance of one answer against another in an effective way?

Essentially, this process, although it may sound straightforward, can quickly become complex. When it comes to investing, putting your best foot forward is the goal. Seek the assistance of a professional who has an objective and thorough outlook on your risk profile. Once they have given you their risk assessment, you are still free to make the investment choices you want i.e. even if they state that you can afford 60% high-risk investments, if you are not comfortable with this you are not obligated to stick to that percentage.

Risks and benefits of creating a joint account

Joint accounts can make it easier to manage shared expenses, but sharing access to your money can be risky.

Benefits

- A shared account will make it easier to pay shared expenses which are common in households with two income earners
- Having one account rather than two means you are paying fewer fees to the bank
- Joint accounts allow each holder to oversee the money available, which is helpful for households who delegate financial responsibilities across individuals

A joint account can best be utilised for shared bills. For example, while you and your partner may have separate savings accounts, one account dedicated for shared bills will make payments easier and consistent.

Risks

- Shared access allows other account holders to withdraw money from the account. Although some accounts require a signature from both holders, others will accept one.
- Sharing an account also means that debts associated with that account are shared. One account holder could be held responsible for another holder's debt.

There is a convenience to opening joint accounts but take this step with a trusted party and discuss how finances will be dealt with beforehand.

We are here to help

Make use of us! This guide is merely a starting point, designed to help you identify areas that might have a significant impact on your personal and business planning.

We are always pleased to discuss matters with you and advise in any way we can.