The Financial Edge

Edition One 2004

Diamond Financial Solutions Pty Ltd, 65 Hume Street, Crows Nest NSW 2065, Telephone: 02 8437 3562
Email: info@diamondfinancial.com.au, Website: www.diamondfinancial.com.au. Authorised Representatives of AXA Financial Planning Limited, ABN 21 005 799 977 an Australian Financial Services Licensee Licence No: 234663.

Ensure your Financial Security **in Retirement**

Proposed changes to complying pensions amd annuities

The government has released a proposed change to complying pensions and annuities. These changes are relevant for anyone who currently receives, or anticipates receiving, age pension support in retirement.

Broadly, the government proposes that from 20 September 2004, the financial services industry will be able to provide a 'complying growth pension' in addition to the existing 'complying pension'. Both of these products will be 50 per cent exempt from the assets test for age pension purposes. The 100 per cent assets test exemption will continue to apply to complying pensions purchased before 20 September 2004.

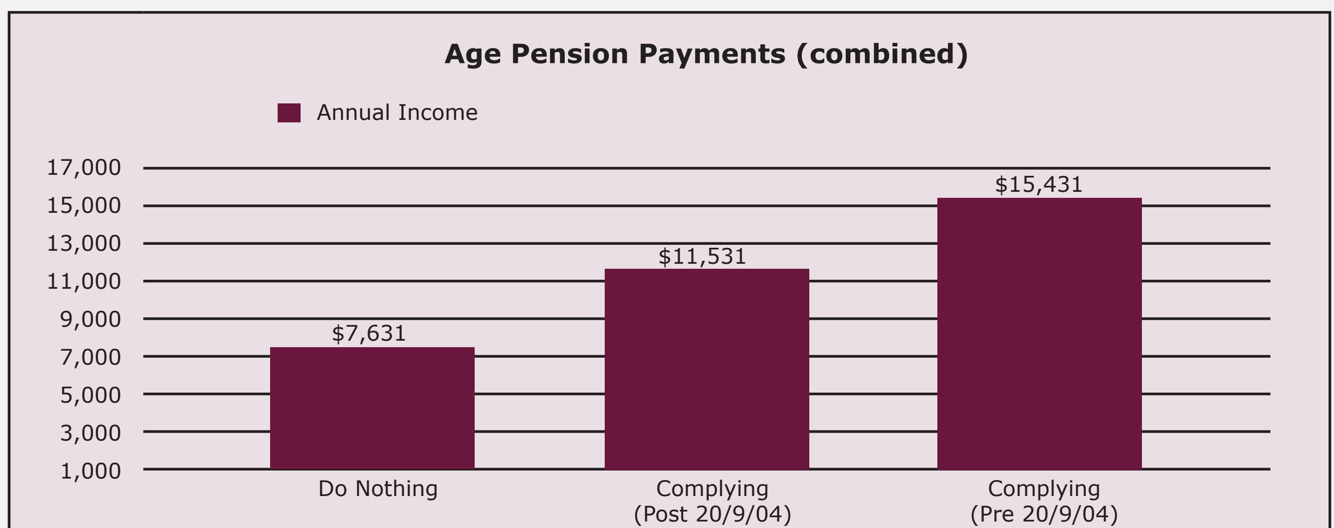
The following case study illustrates the effects of the proposed change, if $100,000 is invested in a complying product.

Jim and Judy have $375,000 in assets, of which $300,000 are financial assets. Based on March 2004 pension rates and the use of the assets and income tests, the current combined payment (including allowances) is approximately $293.50 per fortnight.

Investing in a complying pension product before 20 September will result in a higher pension payment, where the assets test is responsible for any reduction in pension payments. Note - there is also an income test that is applied to determine eligibility and payment level of pension and this may have a geater impact than the assets test for some.

It is important to consider whether or not the lack of flexibility (complying products can not be commuted or turned back into cash) is acceptable to you. Once a complying pension product is activated, rates and other conditions are fixed for the term or life of the product.

Now is te time to get advice.



Financial Planning

This information is provided by AXA Financial Planning Limited (AXAFP) ABN 21 005 799 977, an Australian Financial Services Licensee, Licence No. 234663, a wholly owned subsidiary of AXA Australia and a member of the Global AXA Group. It is believed to be correct at the time of publication, however, no representation of warranty is given as to its accuracy. No liability is accepted by any company within AXA or their respective employees or directors for any statement or opinion or any error or omission or for any loss arising from reliance on the information contained in this document. Investments may only proceed by completing the relevant application form attached to a current Product Disclosure Statement (PDS). Fund managers will receive fees for their services out of which authorised representatives of AXAFP may be paid commission. Neither the return of capital nor the investment performance of any investment is guaranteed by AXAFP. Past performance is not indicative of future performance. Any advice given in this document has not been prepared taking into account your particular investment objectives, financial situation or needs. You should assess your particular investment circumstances prior to making any financial decisions. This taxation information is based on the contribution of present laws and their interpretation and is a general statement only. Individual circumstances may vary.

From time to time we may bring to your attention products, services and other information that may be relevant to you. If at any time you no longer wish to receive information you may opt out by contacting our office.

Budget in Brief

In formulating the 2004/05 federal budget the government's key objective was to boost spending and cut taxes with a focus on middle-income workers and familieis, while not unduy compromising the surplus. The budget contained few surprises as most of the major spending initiatives were leaked prior to the budget announcement. Proposed changes include personal tax cuts and a reduction in the maximum superannuation surcharge rates.

Change in income tax thresholds

Personal income tax cuts will result in more than 80 per cent of taxpayers facing a marginal tax rate of no more than 30 per cent. The changes in tax rates wil occur in two tranches.

- The first tranche occurs on 1 July this year. This involves raising the threshold at which the 42 per cent marginal tax rate applies from $52,000 to $58,000, and the threshold at which the 47 per cent marginal tax rate applies from $62,500 to $70,000.
- The second tranche occurs on 1 July 2005. This involves raising the threshold at which the 42 per cent marginal tax rate applies from $58,000 to $63,000, and the threshold at which the 47 per cent marginal tax rate applies from $70,000 to $80,000.

What does this mean for you?

Current tax threshold	New tax thresholds 1/7/04	New tax thresholds 1/7/04	
Income range $	Income range $	Income range $	Tax rate (%)
0-6,000	0-6,000	0-6,000	0
6,001-21,600	6,001-21,600	6,001-21,600	17
21,601-52,000	21,601-58,000	21,600-63,000	30
52,001-62,500	58,001-70,000	63,001-80,000	42
62,501+	70,001+	80,000+	47

Restricting self-managed super funds

The government is targeting practices that allow individuals to use superannuation funds to avoid tax, shield assets from creditors in bankruptcy, and prevent assets being assessed by Centrelink. Under the measure.

- Accumulation funds will be required to allocate all contributions, and fully vest benefits in a given member; and
- Defined benefit funds and funds providing defined benefit pensions will be required to have at least 50 members.

Reduction in maximum
superannuation surcharge rate
The maximum superannuation surcharge rate will fall from the current 14.5 per cent to 12.5 per cent in 2004/05, 10 per cent in 2005/06 and 7.5 per cent in 2006/07 and subsequent years.

Year	Current	New (proposed)
2003/04	14.5%	14.5%
2004/05	13.5%	12.5%
2005/06	12.5%	10%
2006/07	12.5%	7.5%

Expanding government co-contributions

From 1 July 2004, more individuals will qualify for the government co-contribution will be increased from $1,000 to $1,500 for personal contributions made on or after 1 July 2004. An individual below the new threshold of $28,000 ($27,500 for 2003/04) who makes an eligible contribution of $1,000 will receive $1,500 as a government co-contribution. For income above $28,000, the maximum co-contribution will reduce by 5 cents for each dollar of income to phase out completly at $58,000 ($40,000 in 2003/04).

As announced in February 2004 by Assistant Treasurer Coonan, eligibility for the government co-contribution will be extended to employees who earn less than $450 per month (the Super Guarantee threshold). Under the new eligibility criteria at least 10 per cent of the person's income must be earned as an employee.

Super rules relaxed

Allowing people to access their superannuation in the transition to retirement.

From 1 July 2005, the government will allow individuals who have not retired to access their superannuation as a non-commutable income stream after reaching preservation age.

Preserving rolled-over employer eligible termination payments.

All employer eligible termination payments (ETPs) that are rolled over into superannuation on or after 1 July 2004 will be preserved.

Removing the work test for superannuation contributions for people under the age of 65

From 1 July 2004, there will be no work test requirement for individuals under age 65 to be eligible to make contributions to superannuation. Taxpayers may also be able to claim a tax deduction for their contributions provided they satisfy the 'eligible person' test. In order to qualify for a tax deduction, a person under the age of 18 will be required to satisfy a work test in the year in which the contribution is made.

Compulsory payment of superannuation benefits for people over age 75

Members who have reached age 75 will have to take their superannuation benefit as soon as practicable, either as an income stream or a lump sum. The changes will not apply to people over 75 who still receive superannuation contributions under an industrial award.

Simplifying the superannuation work test rules for those aged over 65

From 1 July 2004, superannuation contrbutions and cashing rules for people aged 65 to 74 will move from a weekly test to an as yet unspecified annual test.

Introduction of Maternity Payment

A new Maternity Payment of $3,00 for each newborn child will be introduced from 1 July 2004. This will increase to $4,000 in July 2006 and $5,000 in July 2008.

This new benefit willbe available to all families, regardless of the family's income, and will incorporate the existing Maternity Allowance and the Baby Bonus. Existing recipients of the Baby Bonus will maintain their entitlement under that program for the full five years, providing the child is born before 30 June 2004.

Changes to Family Tax Benefits
More thn 2 million families are expected to benefit from changes to Family Tax Benefits. Changes include:

- An increase in the rate of payment and a reduction in the income test taper rate for Family Tax Benefit Part A;
- An increase in the income test threshold and a reduction in the income test taper rate for Family Tax Benefit B.

For more information about these proposed changes, see your financial adviser.

Creating Wealth Outside **your Super**

Make your savings work for you

Will regular savings help you achieve your lifestyle goals and if not, what are the alternatives to bank interest?

Dollar Cost Averaging

Dollar cost averaging is a regular payment into an investment. Automatic payments are taken directly from your bank account and placed into an investment , in the same way that you pay off a mortgage. This practice smooths the effect of rising and falling market prices. If you buy all your shares (or units) in a managed fund at one time, and the price falls, you would make a loss. Alternatively if the price rises you would make a profit. You need to be confident that you can predict the future to make a profit in this way. Dollar cost averaging reduces the need to get the timing right.

Gearing

Gearing is another wealth creation opportunity used by many Australians. Gearing entails borrowing money to make an investment. Used by big business and regular investors, the main objective is for the after-tax total return from the investment to be greater than the after-tax cost of the finance.

The interest and other related financing costs on the borrowed funds are usually a tax deduction (see note). As a result, gearing is usually a more effective strategy for those on higher marginal tax rates.

The Leverage Effect

Gearin allows investors to make a larger investment than would be possible using their own funds. As such, it provides the opportunity to significantly magnify the returns from investments. However, this 'leverage' works both ways - if the investment performs well it can enhance the return, but if the investment is a poor one it will magnify te loss (as the inestor is still required to repay the borrowed money).

Consider an investor who can either invest $10,000 of existing funds or borrow an additional $10,000 to make a total investment of $20,000 (Assume that these funds can be invested in $1.00 shares).

Scenario 1: Assuming that the share price rises to $1.50 and the investor sells the shares, the profit/loss situation would be as shown below. In this situation, the non-geared strategy involves 50 per cent capital gain, whereas the geared strategy involves 100 per cent capital gain.

	Non-geared	Geared
Value of portfolio @ $1.50/share	$15,000	$30,000
Less borrowings	$0	-$10,000
Less own funds invested	-$10,000	-$10,000
Pre tax profit (dollars)	$5,000	$10,000
Pre tax profit (percentage)	50%	100%

Scenario 2: Assume that the share price falls to $0.50 and the investor sells the shares, the profit/loss situation would be as shown below. In this situaton, the non-geared strategy involves 50 per cent capital loss, whereas the geared strategy involves 100 per cent capital loss.

	Non-geared	Geared
Value of portfolio @ $1.50/share	$5,000	$10,000
Less borrowings	$0	-$10,000
Less own funds invested	-$10,000	-$10,000
Pre tax profit (dollars)	-$5,000	-$10,000
Pre tax profit (percentage)	-50%	-100%

Since gearing provides a larger exposure to an investment, it accelerates the potential profit or loss. That is, it allows wealth accumulation or wealth accumulation or wealth depletion to be experienced at a faster pace than would otherwise be possible. This means that the overall risk of the investment is increased.

There are many types of gearing facilities, each suiting a different purpose and client need. It is essential you use he right type of gearing facility for your purpose.

These include:

1. Geared share funds
2. Home equity loans
3. Margin lending, including instalment gearing
4. Instalment warrants
5. Protected equity loans and other structured products

Practical Gearing Tips
• Gearing is a long-term (5 years plus) strategy and should not be undertaken simply to benefit from an immediate tax deduction.
• Gearing is most suited to those on higher marginal tax rates and with reliable cash flow.
• Appropriate risk protection insurances, particularly income protection and life insurances, are recommended. This is because a change in circumstances could upset the gearing strategy and force an undesirable early exit from a long-term gearing strategy.
• Don't over gear - have a buffer to protect against margin calls, unexpected events and extreme market volatility. Avoid surprises!
• Prior to undertaking a gearing strategy, ensure other non-deductible debt - such as personal and home loans - is substantially or fully repaid.
• Consider using a variety of gearing facilities and loan types (fixed and variable interest rates over varying time periods). While this is not necessarily a proven method of reducing risks or adding to returns, it may reduce risk.
• Use the gearing facility most suited to your circumstances and the purpose of the loan. Selection of the gearing facility with the lowest cost will enhance your net returns.

Note -The interest and other costs associated with obtaining finance are usually tax deductible. The purpose of the loan must be for investment income production (ie not loans used for personal purposes or your home mortgage) and the borrower and recipient of the investment returns should be the same legal entity. Some protected equity loans and other structural products have tax rulings limiting the extent of the interest rate deduction. Specific financial advice is recommended with any gearing decision.

Salary Packaging - Case Study of Salary Sacrificing into your Super

Let's look at a case study that demonstrates how salary packaging can leave you with more money in your pocket.

Packaging your salary enables you to substitute some of your cash slary for other benefits to reduce your tax liability. Your employer may allow you to package items such as superannuation (super) contributions, company cars, car allowances, mobile phones, car parking and lap top computers. However tax treatment varies across these items. Let's look at a case study that demonstrates how salary packaging can leave you with more money in your pocket.

Jennifer, aged 50 has just started a new job and currently receives a gross cash salary of $70,000 per annum (plus super). Therefore she receives $49,243 net after tax and Medicare Levy.

Jennifer is close to retiring and has decided to spend the next five years making additional super contributions to help increase her retirement savings.

Jennifer has the opportunity to salary package and the benefits offered include car parking and salary sacrifice into super. As Jennifer walks to work she doesn't need a car park, so she elects to package additional super contributions.

Jennifer has decided to salary sacrifice $10,000 from her gross salary of $70,000, to make additional super contributions. This will reduce her annual gross salary from $70,000 to $60,000 and will reduce her tax liability from $20,757 (including Medicare) to $16,032 (including Medicare).

By salary sacrificing or making additional contributions to her super fund, Jennifer's tax liability will be reduced, as she benefits from only paying 15% tax on her super contributions. Furthermore, earnings on her contributions will also be taxed at 15%, rather than being taxed at her marginal tax rate.#

Looking at Jennifer's situation we can see that by using salary sarifice, she is able to save an additional $3,225 towards her retirement savings.

Salary sacrificing is an excellent method to reduce your tax liability. all me to make an appointment to see how you can benefit from packaging your salary.

** Extra contributions are preserved funds, that cannot be accessed until you satisfy the definition of retirement.*

***Tax (if any) on the eventual payment from the super fund has not been shown.*

 # When a superannuation beneti is withdrawn as a lump sum, furtherincome tax may become payable.

Before Package	**$**	**After Package**	**$**
Salary (taxable)	70,000	Salary (taxable)	60,000
Salary sacrifice	-	Salary sacrifice	10,000*
Gross package before tax	70,000	Gross package before tax	70,000
Less taxes		**Less taxes**	
Income tax 2003/2004 rates	20,757	Income tax 2003/2004 rates	16,032
Contributions tax	-	Contributions tax	1,500**
Net value of package	**49,243**	**Net value of package**	**52,468**