



NEWSLETTER
June 2017



Introduction

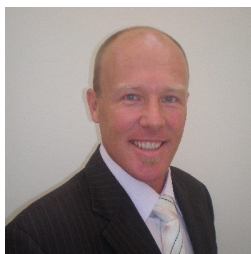
Happy first day of winter!

June is usually a busy month for financial advisers and our clients. The financial year ends this month and that means that anything that needs to be done for the 2016/17 tax year needs to be done now. This year there is a particular imperative – several superannuation rules change on 30 June, which means that many people need to get moving with their super contributions in the next 30 days. We discuss all this in the articles that follow – so read on and please do not hesitate to get in touch if there is anything you need help with before the end of June.

Did You Know... the month of June

June has always been an important month in Australian history. In 1927, legendary bush balladeer Slim Dusty was born in Kempsey New South Wales. His mum called him David. Still on the musical front, the Beatles touched down in June 1964 as part of their world tour. The screaming did not die down until June 1965. More recently, June has been a bad month for Labor Prime Ministers: Julia Gillard rolled Kevin Rudd in June 2010 – and he rolled right back three years later in June 2013. (Bill Shorten was relieved when 1 July 2016 came and went).

And finally, in 1859, Queensland formalized its separation from New South Wales and became its own colony. Happy birthday Queensland!

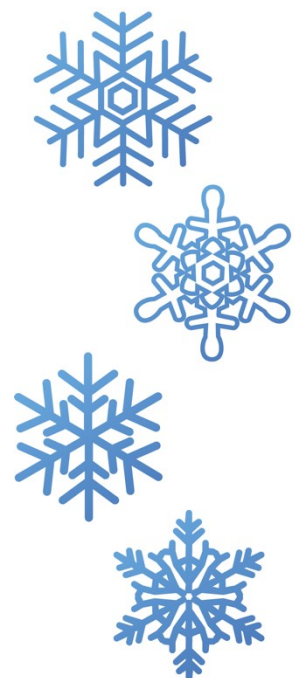


Trevor Boyle

04 2231 0536

trevor@quayfp.com.au

www.quayfp.com.au



MARKET UPDATE

Property Update

In our last newsletter, we discussed the unusual phenomenon of house prices falling in Australia's largest housing market. A minor fall in property prices in Sydney created an overall fall of the same proportion for the entire country - highlighting, if nothing else, the pre-eminence of the Sydney market in the thinking of people setting the economic levers across Australia.

Since then, the Government has delivered the 2017 Federal Budget. The Budget contained at least two measures linked to the residential property market. One of these links was pointed out by the treasurer, although the obvious link between the second measure and property prices seems to have been missed by most commentators.

Downsizing the Family Home

To take the obvious first: one of the measures announced in the 2017 Budget was that, from 1 July 2018, people aged 65 or over who sell their family home will be able to transfer \$300,000 of the proceeds as a non-concessional contribution into their superannuation fund. If that fund is paying an income stream to the member, then earnings on assets within the fund are tax-exempt. Therefore, in most cases, anyone taking up this offer will be able to invest up to \$300,000 tax-free within their superannuation fund.

If a home is owned in joint names, then each owner can transfer \$300,000 of the sale proceeds.

The idea is that older Australians tend to hang onto their family homes because the family home is a CGT-free form of wealth accumulation. For example, if a 70-year-old widow owns a home worth \$1 million, and the home appreciates in value by, say, 7.5% per year, then the owner is effectively earning a tax-free investment return of \$75,000 per year. When the home is eventually sold, there will be no tax paid on the increase in the value of the home.

Under the new scheme, from 1 July 2018, the owner can sell her home, purchase a new

(presumably smaller) property for around \$670,000, pay stamp duty of around \$30,000 and contribute the remaining \$300,000 into her superannuation fund. If the returns on the new property are the same as that on the old property, then a 7.5% rate of growth will add \$52,500 to the value of the new home. Because this is a principal place of residence, no CGT will be payable on this growth.



For the government plan to work, the \$300,000 that is invested tax-free within superannuation will need to grow at a rate slightly above the rate of growth in the property market. This is to compensate for the money paid as stamp duty on the second home. In the long-term, the Australian sharemarket and the Australian residential property market tend to perform in quite close concert (source: ASX Russell long-term investment report for any of the past five years or so). Therefore, people who downsize will likely suffer a little for doing so – and suffer rather more if they do not invest in property growth-matching assets within their super.

Why would the Government encourage this? Well, in theory, encouraging people to sell their family home should reduce supply-side pressures on residential property prices. This should make it easier for people not currently in the housing market – that is, first home buyers – to enter. Certainly, this is what the Government hopes will happen.

We use the word 'hope' deliberately here. It is highly unlikely that this will be the effect of the program. For a start, if people who downsize re-enter the market to purchase a new property, then the increase in supply will be matched by an increase in demand. What's more, the increased demand will happen in a cheaper part of the market – a segment where first home buyers are most likely to be trying to buy.



Secondly, anybody receiving an aged pension is unlikely to take up the offer. As most people know, the value of the family home is exempt from the assets test used to calculate the aged pension. But superannuation benefits are not. Therefore, swapping wealth from a home to a super fund makes people more vulnerable to the assets test.

The \$300,000 additional non-concessional contribution is not subject to other rules preventing people making non-concessional contributions into super. For example, people with more than \$1.6 million of superannuation benefits generally cannot make non-concessional contributions (as of 1 July 2017). But they will be able to contribute money derived from selling the family home.

People in this situation (with more than \$1.6 million in superannuation) won't have their aged pension affected by the movements: they are not getting the aged pension in the first place.



That's why some commentators have observed that moving up to \$300,000 into superannuation may benefit wealthier people for whom Centrelink planning is not relevant.

Unfortunately, the houses that such people are likely to be selling will be worth more than first home buyers could afford anyway. Even more unfortunately, the houses that these downsizers might then want to purchase may well be in the section of the market in which first-time buyers are more likely to be active.

For that reason, it would be very surprising if this measure has any material impact on house prices, and even more surprising if first-time buyers were to receive any benefit from it.

The new bank tax



The second Budget announcement – and one that will have a bigger impact on the property market - is the imposition of a new tax on Australia's five largest banks (that is, banks with more than \$100 billion in liabilities).

A tax of 0.06% is applied to the value of specific liabilities owed by these banks. These liabilities are generally those at the higher risk end of the bank's

activities (for example, deposits above \$250,000 held by the bank - a bank deposit represents a liability from the bank's perspective).

The tax has been scheduled to last at least four years - but if it works, what do you think the odds of it being removed in year five are? The government expects that it will raise around \$1.6 billion per year from this new tax.

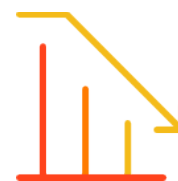
In announcing the measure, the government pointed out that the banks to whom it will apply all make substantial profits. For example, the Commonwealth Bank reported a \$4.9 billion profit for the six months to December 2016.

Perhaps the government is hoping that the banks will simply 'wear' this additional tax and their profits will be reduced accordingly. But that's not the way banks normally operate. Banks enjoy a 'very strong market position.' Everybody needs a bank and moving from one bank to another is a hassle. This creates a somewhat captive market.

This gives banks substantial ability to pass costs on to these 'captive customers.' In our last newsletter, we reported that banks had been able to increase interest rates on certain kinds of property lending (particularly for investors) without much public backlash. They could do this because (i) most people are not investors; and (ii) most people blame investors for at least some of the demand currently pushing housing prices beyond the reach of many. Increasing the cost of borrowing for investors should weaken their demand for property and take some pressure off prices.

That certainly seems to have been the case in May. It would seem very likely that banks will similarly pass the cost of this new tax on to certain customers - customers who don't enjoy much public goodwill. Property investors – that means you!

Therefore, the imposition of this new tax on the banking sector may well reduce demand in the property market, by increasing the costs of participation in that market for purchasers. Strangely, there has been relatively little media commentary about this likely result.



There is, of course, a chance that all interest rates will be affected – even for non-investors. In a blog article we posted last year, we encouraged clients

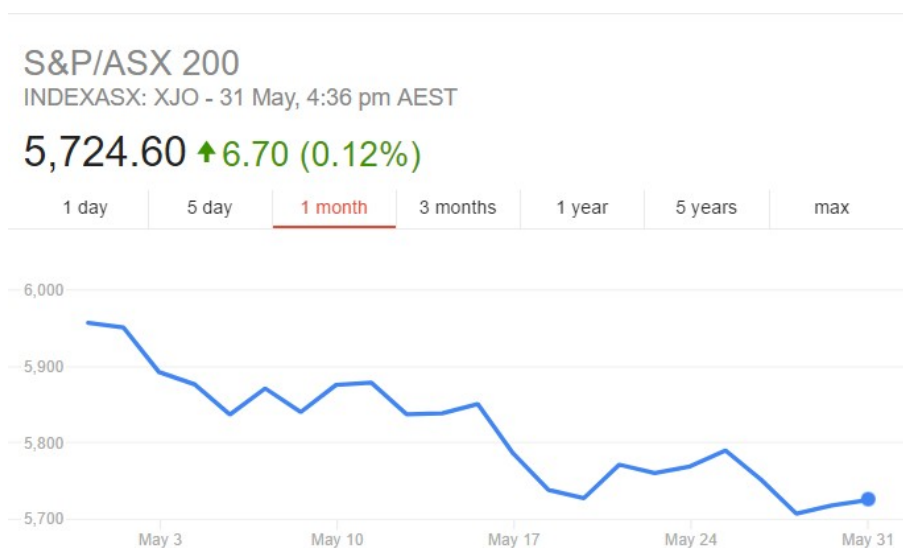
to use the current low interest rate environment to retire as much debt as possible - especially if that debt is non-deductible has been used for private purposes, such as a family home. Following this Budget, we simply reiterate that advice: the best way to cope with rising interest rates is to owe less money.

If you would like to explore ways of repaying private debt more quickly, please don't hesitate to get in touch with us.

Share Market Update

It's now been six months since America voted for its new president. That six months has seen world equity markets perform radically differently to what many people anticipated when Donald Trump was first elected. The Australian market tends to take its cue from the US one and the 'Trump effect' was no exception. Indeed, from a starting point of 5,156 points on November 9, 2016, the ASX 200 rose to a high of 5,956 points on 1 May 2017. That is, in 25 weeks, the market rose 800 points or 15.5%. Add in dividend returns, and that meant a total sharemarket return of around 17% for a period of just under six months.

1 May was the high point of the Australian sharemarket for the entire month of May. The market closed the month at 5,724 points, representing a fall of 3.9% for the month. Here's how Google and Yahoo Finance saw it:



May's fall may have various explanations. One is that it could be a natural correction following a period of abnormally large growth. A second is that it was driven by concerns about the US presidency – especially whether this particular presidency will run its full course.



You may remember that Trump fired the director of the FBI, James Comey, on 9 May. From our position, down here in the world's happiest place, we have no idea why that was done or what the likely outcome is going to be. But it seems that many people in the US are concerned that Comey was fired to stop him finding things out about the US administration. This concern has led investors in the US sharemarket to worry that the President may not be able to continue in office. If Trump being President raised market prices, then Trump ceasing as President should do the opposite. I guess we need to watch this space.

Whether a fall in the sharemarket is good or bad news is not always obvious. If you need to sell shares when prices are low you will be unhappy: you get less cash for your shares. But buyers get a better deal: they pay less for the shares they acquire.

So whether the adjustment to prices in the month of May is good news depends on your plans for June. If you're a buyer (or if contributions are simply being made into your superannuation fund, from where they will be invested into the Australian sharemarket) you should be happy. If you're a seller, less so.

Remember, though, that these monthly variations highlight something that has always been true of the sharemarket: it is hard to predict in the short term. When James Comey turned up at work on May 8 not even he knew he was about to be fired. But in the long run, sharemarkets tend to do as well as the economy in which they participate. And in

the long run, economies like Australia's tend to do well.

The one thing we do know is that sometimes share markets fall. In that sense, the performance in May was predictable. Our focus when providing

investment advice is always to help you plan for these regular 'bad months' so that no particular month is all that important to your wealth.

Who gets your super when you no longer need it?

First published May 10 2017

Our theme this month is estate planning, and so we thought we would start with a quick article about what happens to your super when you die. We know, it sounds grim, but it is not really. After all, the rate of death has remained unchanged for quite a while: we all get one each. And most of us want to die with some money left!



An important thing to remember when it comes super is that you are usually not the legal owner of your superannuation benefits. That

might sound odd, but the assets are actually owned by the trustee/s of the relevant fund. As your trustees, they owe you a duty to do the right thing by you and to manage the assets for your benefit. But, once you have died, it becomes pretty hard to insist on this, that's why it is a great idea to establish a 'binding death benefit nomination' before you go.

Let's pick that term apart to understand what it means. Death benefits are benefits that remain in the fund and need to be paid out to someone when you die. A nomination is a where you tell the trustees who you want to receive your death benefits. The fact that the death benefit nomination is binding means that the trustees of the fund must pay the death benefits as you have stipulated.

It is always worth remembering that superannuation is complex. After all, the rules were dreamed up by politicians and then written up by bureaucrats. One of the complexities is what happens to your death benefits from a tax perspective. Basically, whether these benefits are subject to tax depends on two things: the nature of the benefits and the nature of your relationship with the person who eventually receives them.

If the person who receives your benefits is what is known as a 'death benefit dependant,' then they will not pay tax. A death benefit dependant is basically:

- Your spouse;
- Your child or children if they are aged under 18; and/or

- Any person who was financially dependent on you when you die. This might include, for example, a 21 year old child still living at home.

If the person who receives the benefits is not a death benefit dependant, then the benefits may be taxed. Once again, this will depend on the nature of the benefits within the fund.

All superannuation benefits are divided into one or both of two types: the taxable component and the tax-free component. As these names suggest, tax-free components are not subject to tax when paid out as death benefits, even if the recipient is not a death benefit dependant. Taxable components will be subject to tax if they are paid out to someone who is not a death benefits dependant.

Got that? The point is: if your super will go to someone other than your spouse, your children aged under 18 or someone aged over 18 who is not financially dependent on you, then the taxable component of that super will be taxed.

So, from a tax planning perspective, if your benefits are going to be paid out to someone who is not a death benefit dependant, then it is best if your benefits are tax-free to the greatest extent possible.

The thing is, whether the benefits are taxable or tax-free depends on how they got into the fund in the first place. If whoever put them there got a tax deduction for them (think of an employer making a compulsory super contribution), then the benefits will form part of the taxable component. So will investment earnings that are then generated on these benefits. But if there was no tax deduction claimed when the money first entered the fund (known as a 'non-concessional contribution'), then these benefits will form part of the tax-free component.

Tax-free components are never subject to tax when paid out as death benefits, even if the recipient is not a death benefits dependant. The trick, then, is to maximize the proportion of benefits in the fund that derived from non-concessional contributions. This gives rise to a strategy known as a 're-contribution strategy.' In a re-contribution strategy, a fund member who is

eligible to do so withdraws benefits from the fund and then re-contributes them back in as a non-concessional contribution. This increases the proportion of benefits held in the tax-free component. This in turn reduces the amount of tax that would be paid by a non-death benefit dependant when eventually the member dies.



This really is planning for your beneficiaries. After all, the tax that is being saved was not payable until after you died anyway. But it can be well worth thinking about.

Of course, given the complexity, things must be done right. There are some i's to dot and t's to cross. But it is not too difficult when you know what you are doing. So, if you would like to maximize how much of your super actually makes it to your loved ones, talk to us about whether a re-contribution strategy will work in your case.

The tax advice component of this post was created by Dover Financial Advisers, a registered tax (financial) adviser.

Superannuation Changes on July 1 2017

First published May 23 2017

You probably know the Commonwealth Government hands down its annual Budget in early May each year. It's an exciting time of year for financial planners. Most advisers let their excitement overcome them and race to put material on their website as fast as possible. The Budget is handed down on Tuesday night and the websites get updated on Wednesday morning.

Experience has taught us to do things a little differently. Immediately after the Budget, the media is typically saturated with news of the changes. So we prefer to wait a while before we publish our thoughts. This lets us fully digest the changes so that when we do write about them we are providing a thorough and intelligent response that actually helps our clients choose the best way to respond.

And that was our intention again this year. But guess what? The 2017 Budget was very different. It actually contained few changes that will be relevant for many of our clients. To be honest, this was a major relief: the changes from 2016 were so substantial that we needed a year off!



Between now and the end of the financial year we will discuss the relatively minor changes that the 2017 Budget will herald for our clients. But before we do that, we are going to devote a couple of articles to discussing the really major changes that were announced *last* year, in the 2016 Budget. This makes particularly good sense, because most of those changes take effect from 1 July 2017.

1 July 2017 is coming up fast – but it is not here yet. So if you think that the changes below will affect you negatively, then please contact us immediately to see if we can act pre-emptively and help you make the most of superannuation.

As you read through the discussion below, please remember this: superannuation remains a really generous way of saving for retirement. Yes, most of the changes mean it has become less generous, but 'less generous' does not mean 'useless.' Superannuation remains a critical part of any decent financial plan. Please keep it front and centre in your thinking.

Concessional contributions – from July 1, you can't make as many of 'em!

A concessional contribution is one for which the contributor claims a tax deduction. The flipside of this is that the superannuation fund pays tax of 15% when it receives concessional contributions. The most common type of concessional contribution is the mandatory superannuation contributions that all employers must make on behalf of their staff. This contribution is typically required to be 9.5% of the employee's gross salary.

Self-employed people can also make concessional contributions into their superannuation funds, although there is a little bit of paperwork involved in that process. Unfortunately, it can seem that even that



little bit of paperwork is too daunting: at least 25% of self-employed people have no superannuation at all (source: ASFA).

If you are self-employed, you simply must make sure you use super as much as possible! Talk to us and we will show you how.

From 1 July 2017, the amount of contributions for which a tax deduction can be claimed will be capped at \$25,000 per year. This is a reduction across the board. For people aged over 50, the previous limit was \$35,000 per year. For everybody else, the previous limit was \$30,000 per year.

There is some good news, however. For people with superannuation balances less than \$500,000,

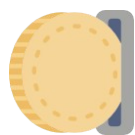
the annual limit will actually be averaged over a five-year period, such that concessional contributions equal to \$125,000 can be claimed across a five-year period. Spreading contributions like this will be particularly useful for people whose income varies each year. This can include self-employed people, people returning to work or taking time out of work for childbirth or other reasons.

From 1 July 2017, most people will be able to make 'personal contributions' into

superannuation. These personal contributions are added to other concessional contributions and the total of all concessional contributions cannot exceed \$25,000. People can simply pay money directly into their superannuation fund. The only stipulation is that you must tell the fund that this is a concessional contribution for which you will claim a tax deduction. (If you do not want to claim a tax deduction for the contribution, then you should identify it as a non-concessional contribution. Please see below).

Non-concessional contributions – you can't make as many of them, either!

A non-concessional contribution is one for which the contributor does **not** claim a tax deduction. The flipside of this is that the superannuation fund does not pay tax when it receives the contributions. Non-concessional contributions are sometimes known as 'after-tax' contributions.



The main purpose of non-concessional contributions is to move money into the superannuation system, where investment earnings are taxed at no more than 15%. Capital gains are typically taxed at 10%, and no tax at all is paid on earnings where assets are being used to finance a pension (although see below for a discussion of the changes to transition to retirement pensions). So, contributing money into superannuation in order to invest often reduces the total amount of tax paid.

Currently, non-concessional contributions are limited to \$180,000 per year per person. People can bring forward up to 3 years' worth of

contributions, allowing them to contribute up to \$540,000 at a single point in time.

As of 1 July 2017, the annual limit for a non-concessional contribution will fall to \$100,000 per person per year. People can still bring forward three years' worth of contributions, meaning that the effective limit is \$300,000 per person over a three-year period.

Not everyone can make a non-concessional contribution. People aged 75 or older cannot make them. People aged between 65 and 74 can only make them if they satisfy a work test. People with superannuation assets worth more than \$1.6 million as at the most recent 30th of June cannot make them regardless of their age.

In summary, if you are considering making a non-concessional contribution into superannuation, then you should talk to us immediately. There is still time between now and 30 June for you to take some advantage of the rules as they currently exist.

The Legal Stuff

General Advice and Tax Warning

The above suggestions may not be suitable to you. They contain general advice which does not take into consideration any of your personal circumstances. All strategies and information provided on this website are general advice only.

We recommend you seek personal financial and/or taxation advice prior to acting on anything you see on this website.

Contact Details

Address	Level 1, 50-58 Moorabool Street GEELONG VIC 3220
Phone	04 2231 0536
Website	www.quayfp.com.au
Email	trevor@quayfp.com.au

Licencing Details

Quay Financial Planning Pty Ltd (ATF Boyle Investment Trust) is a corporate authorised representative (322767) of Consilium Advice Pty Ltd.

Consilium Advice Pty Ltd

AFSL 424974 | ABN 86 158 826 647 | Level 9, 44-48 Hunter Street, Sydney, NSW 2000