Personal Wealth Adviser

Managing your personal finances

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Our Sydney personal wealth management team provides you with a simple solution for your personal wealth needs. We have specialists in wealth management, superannuation, self-managed superfunds, estate planning, debt advisory and insurance services.

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MICHAEL HUTTON
Partner, Personal Wealth Management

WHEN IT'S TIME TO LET THE KIDS GET INVOLVED IN YOUR FINANCES

This is how to plan for a little help as you get older without causing a family feud.

There may come a time when adult children need to become involved in their parents' financial affairs. This must be handled carefully, no matter what the nature of the relationship. Every situation will be different.

It may be true that no one looks after their own money better than themselves. However, financial matters can become complicated, and many people need assistance from financial advisers, accountants, and lawyers to put their finances in order.

There may come a time when adult children need to become involved in their parents' financial affairs. This must be handled carefully, no matter what the nature of the relationship. Every situation will be different.

In other cases, adult children may need to take on a more formal role. For example, adult children might take on the role of a financial guardian, with appropriate power of attorney arrangements.

We've observed many cases where children or another trusted person have successfully integrated themselves into managing the financial affairs of parents or others without any acrimony involved.

This includes organising who pays the bills, which requires access to bank accounts. Failing to pay bills in a timely manner is often an early warning sign that assistance is required, particularly if people have always been diligent in this regard.

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Children might be involved in getting their parents' tax returns and other related compliance requirements organised. They might assist with finding aged care and payment of bonds if needed.

Sometimes adult children will have financial skills the parents don't have, and either do things themselves or start to get involved with the parents in liaising with advisers. This is best done seamlessly over a longer period of time rather than being inspired by a sudden emergency.

Where a family business is involved, early attention should be paid to succession plans or selling the business. We've observed situations where families are surprised at how drawn out these processes can be, so it helps to start succession planning early.

Children, or another trusted person, can also take on the role of trusteeship of the parents' self-managed super fund with appropriate appointment of power of attorney. If that's not a suitable arrangement, they can instead become members of their parents' SMSF, particularly now that up to six members are allowed rather than four. This can work well, but may also create issues if the child members have different investment preferences to their parents, so consider the pros and cons carefully.

For many people, it can be an enormous relief as they age to have their children take care of their financial arrangements. Even for younger wealthy families, involving children in financial matters from a young age can lead to seamless succession planning.

On the other hand, we've also seen circumstances where getting the children involved has been disastrous. In these situations, it's usually that one child gains some level of control over the situation to the chagrin of others, which results in big family fallouts.

That's why early and appropriate estate planning is important in terms of appointing powers of attorney and enduring guardians, which apply while the parents are alive. The parents' will and nomination of executors will be important when they die.

Having the children involved in the parents' financial matters should be at least considered in the first instance before moving on to other options.

Michael Hutton has a monthly opinion piece in the Australian Financial Review. This article first appeared as part of this series on 3 July 2023.

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PRUE CHEESEMAN-GOODES
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HOT PROPERTY: IS NOW A GOOD TIME TO SELL YOUR HOME AND MAKE USE OF THE DOWNSIZER CONTRIBUTION?

An opportunity for those over age 55 to boost their superannuation by making a $300,000 contribution each into superannuation.

If you're considering selling your house and wondering whether it's a good time to do so or if you should wait, it's essential to consider your personal circumstances, the current market conditions and factors that may impact the real estate landscape.

Most locations around Australia still have higher median prices than pre-COVID. Whilst 2022 was a challenging year for property, following a historically fast rise during COVID, property prices in 2023 have been rising once again. Data from property consultancy CoreLogic show that the Sydney housing market still leads other major cities with a cumulative increase since the January trough of 6.7%. A lack of supply has been the main driver of the increased prices, as well as high population growth.

The Sydney housing market increased 1.7% in June, a slower rate than previous months, a sign that the market is slowing with expectations of more rate rises to come. Mortgage stress is a big risk for homeowners who have a large level of debt, and some households are struggling to keep up with their monthly repayments. We are seeing more mortgagees considered at risk and many mortgages are due to come off fixed rates in the next few months, and this might start to show increased supply in the market.

So, as a seller it could be a good time to take advantage of the current conditions while supply is still tight and auction clearance rates remain high. If you do sell, you might be able to make a Downsizer Contribution.

So, you might ask "What is a Downsizer Contribution?"

In essence it's an opportunity to invest and boost your superannuation.

From 1 January 2023, you may be eligible to make a maximum non-taxable contribution of $300k for each spouse if you are over age 55 and make the deposit within 90 days of settlement of a sale (or part sale). To qualify, you and/or your spouse have owned your home for at least 10 years and lived in it as your main residence at some point.

The main reason you would want to put an extra $300,000 each into super is because super is the most tax effective structure for your retirement savings, with a balance of up to $1.9M each currently allowed to be used to start a tax-free pension, i.e. no tax on earnings or on pension payments.

Unlike other contributions, it doesn't matter if you are retired or what your super balance is to be able to make downsizer contributions. This may be the last large contribution you can make to boost your balance for retirement.

I wrote an article last year that outlined the pros and cons of making a downsizer contribution which would be worthwhile reading as there is a lot to think about when considering if you should make a downsizer contribution.

Superannuation contribution rules are complex. It is a good idea to seek advice. If you are interested in learning more about the types of contributions you can make, please contact us.

BETTY PRESHAW
Director, HLB Debt Advisory

WHAT'S THE OUTLOOK FOR INTEREST RATES?

First, the good news. The Australian Bureau of Statistics monthly consumer price index (CPI) rose 5.6% in May, significantly slower than the 6.8% it jumped in April.

It's also the CPI's smallest increase since April 2022, suggesting the RBA's interest rate rises are having the intended impact on inflation.

But don't rejoice too soon. That's because when you exclude more volatile items, such as fuel, holiday travel, and fruit and vegetables, from the CPI to get a view of underlying inflation, the fall is more modest – dropping from 6.5% in April to 6.4% in May.

It's also too high for the Reserve Bank of Australia (RBA), which has consistently emphasised its determination to return inflation to its target range of 2-3%, despite risks to the economy.

As such, several major banks have revised their baseline cash rate forecasts upward and now expect a terminal rate in August of:

- NAB: 4.60%
- Westpac: 4.60%
- ANZ: 4.60%
- CBA: 4.35%

Why are interest rates still forecast to rise?

During a speech at the recent Morgan Stanley 5th Australia Summit, the outgoing RBA governor Philip Lowe warned of the dangers of a prolonged period of above-target inflation.

"High inflation is corrosive and damages our economy. It erodes the value of money and savings, puts pressure on household budgets, makes it harder for businesses to plan and distorts investment. It makes us all poorer and hurts people on low incomes the most," he said.

"If inflation stays high for too long, it will become ingrained in people's expectations and high inflation will then be self-perpetuating."

High inflation expectations can lead to higher wage demands, increasing labour costs and setting off a wage-price spiral.

The risk of this is more pronounced in a tight labour market.

Australia's labour market has remained remarkably strong in the face of interest rate rises, with the country adding 76,000 jobs in May, according to the ABS.

That saw the unemployment rate drop to 3.6%, from 3.7% in April.

Adding to the RBA's concerns is the annual wage review decision from the Fair Work Commission of a 5.75% boost to award wages.

This was higher than many expected, so could, in theory, lead to other workers asking for big pay bumps – resulting in a wage-price spiral.

The resurgent property market

Another wildcard is Australia's housing market. The recent downturn has proved shorter than many commentators anticipated, despite the RBA's interest rate hikes.

Driving this rebound has been a shortage of properties. This is unlikely to improve anytime soon, given Australia's strong population growth coupled with the collapse in building approvals – with recent ABS data showing these fell to an 11-year low in April.

The housing shortage is also plaguing the rental market, pushing rents up at an annual pace of 9.9% in May, according to CoreLogic.

Higher rents have been one of the biggest drivers of inflation in recent months.

When will interest rates fall?

Fortunately, there's a bright side.

Because while Australia's major banks are forecasting more interest rate rises, they are also pencilling in rate cuts in the not-to-distant future.

For instance, NAB, in a recent monetary policy update, said it believed the RBA would begin cutting rates back to a 'neutral' level (of between 2-3%) in 2024.

CBA and Westpac also agree that there will likely be significant interest rate cuts next year.

ROBERT MONAHAN
Director, Estate Planning

ESTATE PLANNING - EVEN BILLIONAIRES CAN MESS IT UP

On 3 February 2023, Justice Boddice of the Supreme Court of Queensland delivered his judgment in a case known as Talbot v Boyd Legal. If after reading this article you are interested in reading the full judgment, the formal reference is [2023] QSC 8. The judgment covers 214 pages, and it is certainly not light reading!

I was one of two independent Lawyers from NSW who were asked to give expert evidence. The court proceedings were the culmination of a very sad story.

In June 2010 an Australian Billionaire, Ken Talbot was traveling throughout Africa to bring his innovative coal technology to the continent when he perished in a plane crash together with ten other passengers. It goes without saying that the tragedy had an enormous impact on his wife Amanda and his four children from his two marriages.

Ken's last will was signed in 2002 when his estate value was estimated to be $130 million. At the time of his passing, however, his estate had grown over ten times to $1.3 billion and he hadn't yet finalized an updated will. Ken had put a lot of thought into his 2002 will and included some interesting preconditions on each of his children before they were to be given a slice of their inheritance at age 30 years. The preconditions were:

1. They had to provide written confirmation from three independent doctors that they were not alcoholics or drug users; and

2. They have had to pass a diploma course for company director in Australia.

Interesting as those preconditions may be, they are not relevant to the lessons to be learnt from the case. Starting in 2006 Ken's Lawyer suggested to him on several occasions that he should review his Will. Ken's business interests were rapidly expanding, and in 2008 an investigation was taking place concerning an allegation that Ken had bribed a Queensland State Minister. Whilst steps were taken from time to time to update Ken's Will, it had not been finalised by the time of his death.

Ken's 2002 Will appointed an American friend as executor. Ken's wife and children felt the friend was not suitable to administer the estate. The friend was asked to give up the executorship. Apparently, he offered to do so if they paid him $20 million. Ultimately, he agreed to accept $10 million. Ken's Lawyer, Bill Boyd, who prepared the 2002 Will agreed to take over the administration of the estate.

Some time later, Ken's widow, Amanda, sued Bill Boyd for negligence. Had Ken updated his Will as he indicated he had intentions to do, Amanda would have been better off financially. She alleged Bill was negligent for failing to finalise a new Will, and for decisions he made in the administration of the estate. Following a three-week hearing, Justice Boddice decided Bill was not negligent.

I was once told by a Judge that your Will is probably the most important document you will ever sign, because it gives away everything you own. Accordingly a review of your Will should not be placed at the bottom of the 'to so list', and if you do have a Will, it should be kept up to date with your wishes. If your wishes change, so should your Will. Whilst very few of us will end up billionaires, the same rule applies to billionaires and paupers, 'You can't take it with you'.

Had Ken given a greater priority to keeping his estate planning up to date, his family could have simply mourned his loss without the emotional and financial cost that resulted from his lack of action.

HELENA YUAN
Director, Tax Consulting

DO I NEED TO PAY TAX ON THAT BIRTHDAY GIFT FROM AN OVERSEAS RELATIVE?

Do I need to pay tax on that birthday gift from an overseas relative?

You won't be surprised to hear that there is no simple answer to this seemingly simple question.

It is entirely possible that the $50,000 Aunt Jane in New Zealand gave you for your milestone birthday is not tax-free to you as you first thought.

Is it a genuine gift/loan?

Broadly, if a gift of money or property was a genuine gift or loan from a foreign related entity or relative, it is not considered as assessable income and you do not need to pay tax on that amount.

The ATO has published guidance on what it considers to be a genuine gift/loan. The ATO looks for substance over form of the transaction, whether the characterisation is supported by appropriate documentations, the ATO may also look at evidence the donor's capacity to make the gift from their own resources depending on the size of the gift and the nature of the relationship.

At the end of the day, when the ATO knocks on the door, it is your responsibility to provide evidence to prove that the money or property you received from overseas is a genuine gift/loan.

So it is not just a gift, what do I need to do?

Continuing with our example of Aunt Jane's $50,000 gift of money, life gets a bit more complicated if the $50,000 came out of her NZ trust as a trust distribution to you.

In this case, you may need to include some or all of the $50,000 as your assessable income depending on the nature and characteristics of this distribution:

- Whether the trust derived the $50,000 in the same income year that it was distributed to you
- Whether it was sourced from NZ capital gains
- Whether it was sourced from the trust corpus (the trust settlement sum)

On top of the income tax that you have to pay, you may also be liable for a special interest charge if some or all of the $50,000 amount has not previously subject to tax in Australia or in a listed country .

As illustrated in the above example, it is important that you ask Aunt Jane to provide documentation that can identify and support the sources and components of a trust distribution to you and maintain documentation.

Would the ATO know about my 'gift' form overseas?

The ATO has access to data a variety of sources, includes:

- AUSTRAC shares information about international funds transfers with the ATO readily and regularly and the ATO uses the data to match information reported in the tax returns
- For those Australians with income from or assets in low tax jurisdictions such as Jersey, BVI, the Cayman Islands, the Australia Government has tax information exchange agreements to exchange tax information in case of a tax investigation.
- Greater availability and access of data coming out of OECD initiatives

The ATO increasing its scrutiny over undisclosed offshore income. More recently the ATO issued an alert (TA 2021/2) in September 2021 signalling the ATO's audit focus in the coming years.

Disclosure of overseas assets

There is a requirement to disclose to the ATO in an individual's Australian income tax return if during an income year the person owns or has an interest in assets located outside Australia which have a total value of A$50,000 or more. This disclosure allows the ATO to collect information in relation to whether the individual has undeclared any foreign income.

Key takeaway

Money from overseas is most welcome, at the same time you express your gratitude you will also need to consider whether you need to pay tax on it.

If you would like further information on issues covered in this article, we are more than happy to assist.

1 Listed counties are Canada, France, Germany, Japan, New Zealand, UK and USA

LINDZI CAPUTO
Director, Personal Wealth Management

LAST CHANCE FOR $25,000 SUPER DEDUCTION

For those with a super balance under $500,000 the 2024 financial year is the final year unused concessional contributions from the 2019 financial year can be applied.

The concessional contribution limit was $25,000 for the 2018/19 year. If a portion of this limit was not used between 1 July 2018 and 30 June 2019 it could then be carried forward for a period of 5 years where a super balance was under $500,000. Any contributions leftover from the 2019 financial year must now be used by 30 June 2024, or they will expire and be lost.

If no contributions were made in the 2018/19 year, this year may be the final opportunity to add that extra $25,000 to superannuation and claim a tax deduction.

Using carried forward concessional contributions can be highly effective in reducing taxable income particularly in years where income is higher than usual. This could be due to the sale of an investment property, receipt of a bonus or large capital gain from the sale of shares. Taking this opportunity to catch up on unused contributions can be a worthwhile boost to a super balance.

Maximising deductible contributions in the wealth building years is crucial to building a strong superannuation balance by retirement and can be very tax effective. When retirement is 15 to 20 years away, it can be difficult to see the benefit to locking away savings in superannuation. The benefits of a solid tax deduction and longer-term planning can outweigh these concerns where cashflow allows.

A disciplined contribution strategy should be a key part of the overall wealth plan during the high-income earning years. A high income doesn't necessarily equate to wealth. It is rather the ability to save and then do something meaningful with those savings that will determine wealth.

Superannuation is the most tax effective place for wealth to be invested in retirement years, as earnings are tax free once a pension is established. Individuals can now have up to $1.9 million in a tax-free pension account (up from the previous limit of $1.7 million). A pension balance of $1.9 million equates to a tax-free income in retirement of $95,000 per year, based on a 5% drawing from age 65.

A consistent and tax effective approach to building one's super balance will ensure wealth can build throughout career years in the concessionally taxed super environment with that wealth then being well structured in retirement years.

For example, adding an extra concessional contribution of $5,000 to superannuation each year from age 40 could add $130,000 to super by age 60, assuming a starting balance of $200,000 and an average rate of return of 5% after inflation at 2%. It would also lead to a tax saving of $1,200 per year, which is a return of 24%. In addition, that wealth would then be invested and earning an income over the long-term.

Tips to make the most of your concessional contributions:

- Check your contributions history by asking your accountant or checking myGov.
- Catch up on unused contributions before your super balance exceeds $500,000.
- If you plan to claim a personal tax deduction, make sure you lodge a deduction notice with your super fund.
- Consider Division 293 tax if your income is expected to exceed $250,000.
- Seek advice as contribution rules are complex.

JONATHAN PHILPOT
Partner, Personal Wealth Management

WHY AUSTRALIANS SHARES COMMAND A LONG-TERM PERSPECTIVE

It is futile for investors to predict Australian share market returns within six or 12 months – instead, they should look well beyond the one-year horizon to properly assess how shares are likely to perform.

After the initial COVID-19 lockdowns in March 2020, no-one could have predicted the share market would rise by 37 per cent over the next 12 months. This illustrates the inherent risk of a short-term focus towards investing, particularly in shares.

Any investment in the share market should last for a minimum of three years, however history will tell us the real benefits of an investment don't often materialise until well after five years of being in the market. Ideally, the smoothing of share market volatility over time and the narrowing of likely outcomes with each passing year means investors should focus on ten-year forecasting, as this provides a more accurate reflection of market cycles and also allows for likely volatility.

However, the share market shouldn't be viewed as a 'set and forget' investment approach. Asset allocation should be reviewed every couple of years to ensure they are maximising the market value as prices can fluctuate considerably during this time.

When contemplating ten-year forecast returns, investors can make gradual changes to their asset allocation; the share market will not become a sell overnight! This will mitigate any emotionally-charged decision-making that can typically occur after a crisis.

For Australian shares, international shares, property or fixed interest investments, expected returns will ideally be forecast on a five year-plus horizon. Using this timeframe, the expected return for Australian shares over the next five years and beyond is around eight per cent per annum. A large portion of this return – around 5.5 per cent – is the dividend yield plus franking credits, while the remaining 2.5 per cent will come from growth in share prices.

This is an attractive return compared to investing in term deposits, for example. Even though the Reserve Bank of Australia's cash rate has gone up from a mere one per cent at the beginning of 2022 to now be over four per cent, it's likely we are near the end of this period of continuous interest rate hikes. In fact, we even think interest rates could even start to drop in the next few years and expect a term deposit investor will have an average return of 3.5 per cent over the next five years.

While the expected return of Australian shares remains 4-5 per cent above the risk-free term deposit rate, investors should continue to favour taking on some risk in their portfolios and building up Australian shares.

It is not until the Australian share market rises a further 30 per cent before the outlook for Australian shares starts to look similar to term deposits. At this point, if it was to occur in the next couple of years, investors should consider reducing their exposure to Australian shares as the market is moving into overvalued territory.

These changes to the portfolio can occur gradually in ten per cent increments as overvalued markets will often stay overvalued and continue to rise for several years. Quite often, large movements in asset allocation, such as selling all your Australian shares and moving to cash, will have a big impact on the portfolio's performance.

The lesson here for investors is they must accept it is almost impossible to pick the tops and bottoms of markets. However, realising when the share market is in cheap or overvalued territory will greatly assist with good decision-making when it comes to asset allocation.

But most importantly, investors shouldn't be thinking, 'What's going to happen over the next six to 12 months?', but rather, 'How long do I wish to invest for, and what do I want to achieve?'.

Disclaimer
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