

# QUARTERLY INSIGHT

InterPrac Financial Planning Newsletter Edition 1 2020

## Welcome to a new decade!

In Financial Planning we tend to focus on short, medium- and long-term client goals and objectives.

Short term goals tend to be 12-24 months, medium-term a decade, and long-term goals to retirement, a lifetime, or inter-generational.

From a medium-term perspective, it is often good to look backwards to understand just how quickly deferring savings decisions can pass, and why time in the market rather than market timing is so important.

If you would like to sit down to review your last 10 years, and update your current plan for the next short- or long-term goals for you or any other family members, we hope this newsletter gives you some reason to make this decade a financial success.

Unfortunately, the year has started with both tragedy and personal triumph with bush fires, wild storms sweeping our great country as well as a deadly virus breakout at this stage in parts of Asia.

Australians have reached deep into their pockets to assist those impacted, particularly those who have been left homeless, lost businesses, loved ones, or live in a community that may be in a form of recession for up to a decade in some instances.

Insurance companies have been fielding record levels of claims for fire and storm damage and as advisers we hope the homes, fire and storm randomly selected, were those homes fully insured and a greater percentage than we have seen in many other tragedies or previous catastrophes

Insurance whether it be life insurance, income protection insurance, business insurance or just a typical home and contents policy vary dramatically between each other.

Insurance purchased directly and not from a professional is often found to be inadequate only after an event like we have just seen.

Many of our clients have either suffered directly or indirectly and our thoughts are with those impacted and fortunately the better insurers have been fast to act and provide positive outcomes for those under financial stress.

In this newsletter we have discussed numerous subjects, but in relation to those directly impacted by fires, who might not have had insurance, there is scope to get early access to some of your superannuation in certain circumstances.

We have discussed this in brief and offer any friends or families you know that have been impacted with an advice line.

In fact, if you have any questions or queries about how you or your business might be affected by anything you see in this client update, please reach out to our office for further information.

I hope you enjoy the newsletter and look forward to bringing you more updates as the year progresses, and wish you well for another big year ahead.

We have attached a short schedule so you can assess your own insurances to see if you are happy remaining uninsured in some areas and if not, wish us to assist in plugging the gaps of your own family's risk.





# Reviewing your Super

Results for the calendar year 2019 in superannuation have been very good for those who had weightings in property as well as International and Australian equity investments.

Bonds and cash which are considered the safe haven were significant under performers and appear as though they are going to stay that way for longer than most analysts thought when interest rates began their fall. Looking at who was the best performer last year and then investing in it, and selling the under performers, is a trap the inexperienced often fall for. Superannuation is a long-term investment and getting the asset allocation correct, is the key to maximizing returns that suit each client's risk profile.

We would argue those in accumulation mode, with more than 10 years to retirement, are taking far too much risk by now having high bonds and cash weightings and should look to review how much cash and bonds is too much. We would argue that 10% is too much for a balanced risk profile in accumulation at this stage in the investment clock.

This month the ASX 200 Index cleared 7000 points based on the back of optimism that global growth will pick up in 2020. Analysts are tipping local companies will deliver modest earnings per share growth over the 2020 financial year, with fully-franked dividend yields likely to remain attractive. Cash and bonds, the income-producing staples of retiree portfolios, performed comparatively poorly at 1.5 per cent and 4.4 per cent, respectively.

On the upside, lower inflation (both actual and forecast) means that although investment returns are likely to be lower, real returns are not falling as much as people think and the spending power associated with a given level of

investment return is higher than previously assumed.

The upshot of lower for longer is that previous assumptions about how much superannuation one needs to retire, may not stack up. If in retirement, you elect to reduce exposure to risk assets, the strategies of retirees in particular may need to be revised to reflect this new normal.

Let's look at a simple example. Shirley has a super balance of \$500,000 and invests half in Australian Bonds and half in Australian shares. Based on the average market return of 11.9 per cent over the past 50 years, Shirley could have expected to receive a comfortable retirement income (\$43,000 a year for a single person according to the Association of Superannuation Funds of Australia's retirement standard) for 18.5 years.

However, for retirees in 2019, with returns calculated at 4.9 per cent, the money is likely to run out five years earlier (that is, after 13.5 years rather than 18.5 years). The bottom line is retirement savings won't last nearly as long as they have in the past if the allocation is in this realm.

Note that this example does not include the means-tested age pension, which would serve to supplement income once the retiree's balance dipped below a certain level. Even so, it's a powerful illustration and the sort of conundrum that's keeping people up at night.

The group we might call "super accumulators" have time on their side.

People in this group are still working and contributing to super and to prosper a well-diversified growth option would have received higher-than-expected returns over the past five to ten years indeed and calendar year returns for 2019 look to be extraordinarily large due to the significant cut in global interest rates. In one sense, if you are investing for longer periods now in growth options, you can bring forward returns, so to the extent that investors can 'save' these higher returns and they are well placed to withstand a probable reduction in future returns.

The maximum deductible (salary sacrifice super) contributions is the best strategy to take advantage of.

Retirees in draw down or pension phase are much more susceptible to the ill effects of lower for longer because stashing extra money in super is typically not an option. A key question for this group is whether to reduce spending, which means downgrading lifestyle expectations, or changing investment strategy. The first decision is to ensure you have your investment portfolio suitably diversified with enough exposure to higher-returning assets and that is where we assist.

If you are not sure, let's get together and discuss where your superannuation is in respect to your retirement goals. We may specifically have to talk about your current risk profile in respect to your superannuation investment. As we have discussed with all clients, investors should not chase

higher returns and should be very wary of products and strategies that promise unusually high returns.

It's important to think about 'saving' recent strong gains in your portfolio, thereby boosting capital and enabling you to tolerate lower prospective returns. In a recent article, former treasurer Peter Costello who chairs the \$166 billion Future Fund, recently warned that record low interest rates were pushing investors into riskier financial products. Some, he said, were like the collateralised debt obligations that caused all the trouble during the 2008 global financial crisis.

The accumulators may defer adding to super now but, the options when a superannuation balance is not enough at a time when you cannot save and interest rates are low and you have to decide whether you can make adjustments to your lifestyle and accept that returns from the defensive side of portfolios are going to be lower than the past decade or two, or take on more risk hoping markets continue to be strong knowing that if they do not, your reliance on the government age pension comes sooner. Spending less is the other option. People can start to adjust their spending based on their forward-looking returns.

*If we have not already, and you would like to discuss your superannuation planning whether it be a review of your work super, or parked rollovers, please call, the clock is ticking, and interest rates in our view are staying low for quite some time.*





# The Pyramid of Financial Success

When we talk to clients about financial planning, it is all about you and not generic.

The process of providing a financial services guide is to let you know how we provide advice, what we charge and what the financial planning process is. This includes reviewing your current situation, providing you with a written advice document and setting up a long-term support strategy to help you reach the specific advice outcomes you sought.

On occasions it is good to look at advice from a generic viewpoint, and this can help look at the financial planning process from an aerial viewpoint.

If we use an investment pyramid it is important to understand your top priorities at the base of the pyramid.

It may look something like this.

## The base of the pyramid is to actually set a financial goal.

A lot of people start a day with a to-do list.



We all get interruptions and these include phone calls, answering emails, reading our newsletter that just popped in to your email box, chatting with colleagues and all of a sudden, the day is half gone.

Trying to build and protect wealth without defining long-term goals is similar. Rather than just having a goal of 'wealth accumulation', take a step back and articulate the specifics of what you're trying to achieve, when you'll need the money, and how much.

Is it building a nest egg for children's education? is it ensuring you have enough capital to have the same or more income in retirement than when you are working, do you want to buy a bigger house within the next five years?

Only you know, and this is what we believe should be the base of a financial pyramid.

## The next band: managing your saving and spending

The second level of the pyramid is the hard stuff.

Many planners call it paying yourself first, others call it budgeting, whatever the terminology it is boring, requires discipline, desire and dedication to a goal.

It is easy to put it off, and you'll be hard-pressed to make up for a shortfall if you haven't saved enough. This is key to ensure that your savings rate puts you on track to achieve the above-mentioned goals. This concept matters long after you've stopped saving, too.

Retirees are obsessed with the topic of spending rates and for good reason. The difference between a 4% and a 6% withdrawal rate can be enormous when it comes to the viability of a retirement plan - especially when interest rates are so low.

## Choosing your asset allocation

Once you have decided to set a goal, and have determined how to save for that goal, the next key to a sensible financial plan is to get the right asset-allocation mix for you.

A portfolio that consists entirely of cash and short-term bonds will exhibit very few fluctuations but when interest rates are as low as they are today, it is hard to get the benefit of compounding. Cash in this environment is peace of mind and to fund very short-term goals. Over time, however investing in cash in the present market is an investment in wealth reduction.

Your ability to accept risk differs and getting the correct asset allocation is paramount to your returns. It is not up to your planner to define how much risk you should take, but a combination of education and understanding to match your risk appetite to the appropriate mix of investment thematic that will deliver your best outcome.

The achievement of long-term goals is all about getting the asset allocation right for the time in the cycle you invest. The more time you have, the greater risk you are capable of taking. In financial planning time is the thief of performance. Success is more about time in, not timing of investment.

## Managing your own behaviour

On the point of time in, rather than timing, managing behaviour is so important.

We know fear and greed cost the majority of investors. Most people buy when markets have already risen, and sell when they fall. The customer with a goal, a savings plan, the correct asset allocation can reduce the fear and greed factor if it is correct for your risk profile.

Many financial advisers say one of their most important contributions to their clients' financial well-being is to help them manage their emotions and stick with their plans through good and bad market environments.

It's important to identify and manage your own potential behavioural hang-ups, such as a tendency to be too risk-averse for your life stage or to have more confidence in your investing abilities than is warranted.

## Tax efficiency

Many advisers focus on tax efficiency ahead of the other levels of the pyramid, and this is not efficient.

Paying too much tax is dumb, but also investing for tax only reasons is dumb. Paying attention to tax efficiency encompasses a very broad and important set of issues, including taking advantage of tax-advantaged superannuation accounts, using low turnover funds, proper asset location, and employing tax-efficient withdrawal strategies during retirement is sage.

In fact, tax-efficient decision making is one of the key factors that add value in the financial planning process. This is where you talk to us, but getting the first part right comes well ahead on how to pay less tax. One way of paying less tax is losing money.

## Investment selections

The selection of the investments is our last function. When you do not see us, we are busy meeting fund manager after fund manager, insurer after insurer, bank after bank to understand one investment product against another.

In our case we have over 3000 investment funds to select from that are approved by our investment committee as well as access to every life insurer. You do not need to know the difference between each because that is a part of what we offer to you.

To determine which manager or insurer product best serves your risk profile and needs. This for you is the least important albeit often the fun stuff and why we have seen so many move to manage their own self-managed super funds or portfolios.

The investment selection placement does not form the basis of the advice. The advice is the understanding and assistance in setting of goals, understanding how to budget to save for them, establishing the right asset allocation, ensuring the investments are tax effective and then finally choosing the investments, insurance and product strategy that is in your best interest.

We know there's a big difference between investing with a high-quality fund than a C-list fund but for us that is the easy part. We already know these answers and are impartial to this part of the process. Investment selection appears at the top because it needs to be informed by the factors beneath it in the pyramid.

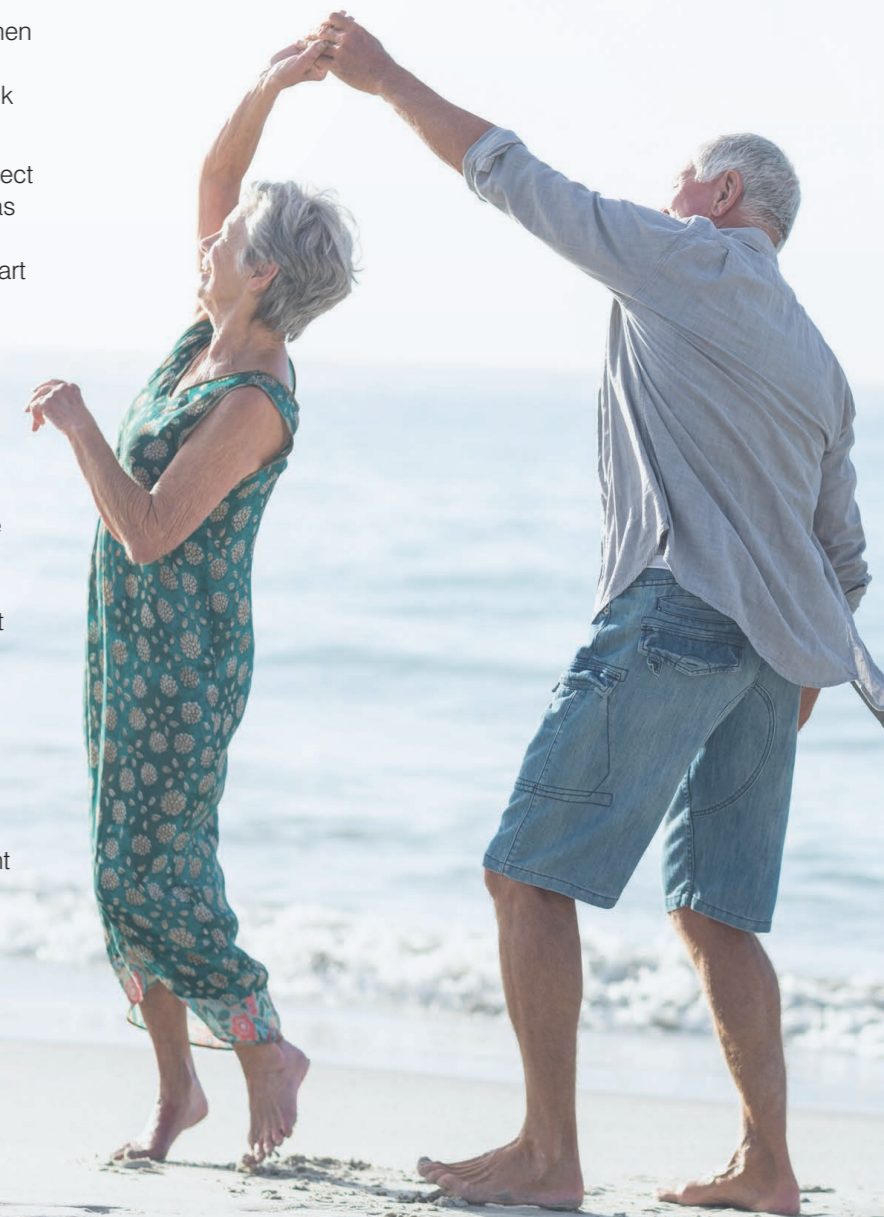
It's not always the case that tax considerations will trump your investment selection, but taxes should be an input in what securities you choose, as should your allocation needs, your expectations for the investment (having the right expectations should ameliorate bad behaviour), and the rest of your financial plan.

Once those factors point the way toward a certain category of investments, you can then look at fees, management, and other investment-specific hallmarks of quality.

## Review

Often on reading the process once again, you may wish to do a further review your current circumstances.

*If you do, give us a call and we can sit down to discuss your very own pyramid.*





# Natural disasters and access to superannuation

This article was written by Olivia Long and appeared on Morningstar.

The impact of Australia's ongoing bushfire crisis is devastating. Not only are Australians losing their homes and entire belongings, but many are also hit by the loss of their business or means to generate an income. They may be in urgent need of cash as a result, and charitable and government support will be limited. In the first instance, people impacted may be entitled to a disaster recovery payment and should contact Centrelink.

The disaster recovery allowance is a short-term payment to help anybody if a declared disaster directly affects his or her income. You can access it for a maximum of 13 weeks and is payable from the date you lose income as a direct result of the bushfires.

## How does early access work?

Whilst the Australian Taxation Office (ATO) does allow for early access to superannuation under compassionate grounds or for those suffering 'severe financial hardship', it is recommended access to super remains a last resort to those in need. This is due to the nature of superannuation and its intended use to 'provide an income upon retirement'. It may also be difficult to put money back into super after it is taken out.

Members of SMSFs and large super funds, however, may try to access their superannuation due to severe financial hardship in addition to the disaster recovery payment. A super withdrawal due to severe financial hardship is paid and taxed as a super lump sum.

The minimum amount is \$1,000 (unless a super balance is less than \$1,000) and the maximum amount is \$10,000.

Superannuation members can only make one withdrawal because of severe financial hardship in any 12-month period. Another option available to those eligible is to commence a transition to retirement pension, called a TRIS. It allows access to super without having to retire or leave a job. A TRIS permits super members to draw down a maximum of 10% of their super account balance during a financial year, which can be used to fund expenses. In an SMSF, funds are accessible immediately.

To be eligible, a member must have reached their preservation age (if another condition of release has not been attained). For those born before 1 July 1960, the preservation age is 55, but the age increases for those born after that date. For more details, see the ATO website.

## Sympathetic judgement needed

Given the magnitude of the devastation caused by the bushfires, the Federal Government should allow early access to super to assist those impacted during these horrific times.

*If you have been impacted call our office and we can discuss your situation and contact the trustee of your super fund*



# Insurance - are you self-insuring?

Insurance is not compulsory and each of us has a choice to transfer the risk to an insurer or self-insure.

As a generalization the population has tended to fully insure, or at least attempt to fully insure a business, home and motor vehicle more regularly than they have life insurance (even though you can add it to your super).

Trauma insurance, income protection and even health insurance are more commonly left self-insured. The government provides some protection on this front albeit inadequate to fund an existing lifestyle.

The government provides tax deductibility of premiums to encourage employees, and the self-employed to take out income protection as well as provide Centrelink benefits for those who do become disabled with insufficient assets or other income to support themselves if they are self-insured.

On the health insurance front, the government is far more supportive with a very good Medicare system and a tax system that provides tax relief through a tax rebate to those who take out private health insurance. The number of self-employed people without income protection is the biggest concern we see as planners. Self-insuring income is a high risk.

Income protection protects against an accident or illness paying 75% of income is well above 60% and we see this as a heavy vulnerability to families with a business owner uninsured. The question to ask is, if I suffered a total loss, what impact would self-insuring have on my life.

Often the land value where a total loss of a family home occurs is similar to the value with the property intact.

That is not a reason to self-insure in those cases just an observation, and does allow for some form of protection in that they can sell the land and suffer little on paper loss.

In these circumstances the insurance policy wording protects the insurer so you cannot have a double win, and take the cash to rebuild as a claim and then sell the vacant lot. In years gone by when replacement was not compulsory in all insurance contracts self-arson may have been more prevalent.

The home contents are often an area people are under insured as far too many of us don't actually realize the full replacement value of our home contents assets and most insurers offset the actual loss by the percentage of under insurance.

If your contents are actually worth \$100,000 and you insure for \$40,000 you only have 40% of a \$40,000 insurance claim, which in itself becomes a form of self-insurance in some cases. Motor vehicle is similar, the difference between agreed value and replacement value policies can be substantial.

Trauma insurance is a relatively new form of personal insurance, that covers us if we have a major medical trauma such as a heart attack, cancer, stroke and pays out a lump sum amount to assist in our recovery without the added stress of needing to get back to work or our business at a time we should be resting.

These days with improved medical attention getting back to full work is far earlier than it used to be, and having a trauma policy relieves the need to do this, where other forms of insurance may not.

It is a comprehensive field and if you would like to discuss any area of insurance, we have specialists who can assist.

## Don't sell your home when you are a non-resident

The law now provides that if you sell your home in Australia, you will not get any exemption for the capital gain made if you are a non-resident of Australia at the time. An exception is if you have been a foreign resident for a period of 6 years or less and certain life events have occurred i.e. your death, or divorce (and equivalent) or terminal illness, or the death or terminal illness of your spouse, or child under 18 years old. Transitional provisions provide an exemption if the dwelling was held before 9 May 2017 and sold on or before 30 June 2020.

## Special rule for high-income employees with more than one employer

If you are an employee with more than one employer and salary exceeding \$263,157, your employers' contributions will result in you breaching the \$25,000 concessional contributions cap. To avoid this, you can now apply to the ATO for an "employer shortfall exemption certificate". An employer who receives this certificate will not have to pay SG for you. If you apply for this certificate for your employer, we recommend you negotiate to receive additional cash or non-cash remuneration, instead of SG contributions.

## Basic Personal (Non-business) Insurance Check List:

Class of Insurance	How much
• Home (Building)	• Full Replacement Value
• Home (Contents)	• Full replacement Value
• Home (Personal Effects)	• Specific items like jewellery
• Motor Vehicle	• Comprehensive
• Life Insurance	• Sufficient to support dependents
• Income Protection Insurance	• Up to 75% of income to age 65
• Trauma	• Sufficient to fund a recovery period
• Health	• Full Cover if you want private





# Dealing with debt

Australia's household debt is among the highest in the world and rising, thanks largely to worsening housing affordability and plentiful consumer credit.

## So how do we measure up and should we be worried?

Most global comparisons measure total household debt as a percentage of net income. At last count, Australia's household debt to income was almost 200 per cent.

Is that a problem?

## Good debt vs bad debt

Debt is not necessarily bad if it's used to grow wealth and you have enough income to service your loans. After all, borrowing to buy a home has been the cornerstone of wealth creation and financial security for generations of Australians. Borrowing to invest in assets such as shares and property that repay you over the long term, rather than the reverse, is also regarded as good debt.

Bad debt arises when you borrow to pay for things that don't provide a financial return and that you probably couldn't otherwise afford, such as that overseas holiday you paid for with your credit card. Unless you can afford to repay the debt in full when you get home, the debt can blow out and linger for years.

Most people take on debt in the expectation that the assets they buy will grow in value and their income will increase over time, reducing their debt burden. But what if these expectations aren't met?

When debt is cheap it increases the likelihood of investments outperforming the cost of holding the debt.

## Wages not keeping up

One challenge with high household debt, which has increased by 83 per cent in a decade, is when income does not keep up.

As a statistic wage increases have been stuck at or near 20-year lows since 2015. It's currently tracking at around 2.1 per cent, barely above inflation of 1.9 per cent and half what it was a decade ago.

Households are generally considered to be under financial stress when their mortgage repayments or rent account for more than 30 per cent of their income.

In the December 2017 quarter, it took 31.6 per cent of the median family income to meet average loan repayments and 25.8 of median income for median rent payments.

So, while interest rates remain low, now is the time to take control of your finances and get on top of debt.

## Tips for dealing with debt

**1. Do a reality check.** Add up all your borrowings and the interest you are paying on each. This includes mortgages, investment loans, personal loans and credit cards. While the mortgage is likely to be your biggest debt, it's also likely to carry the lowest interest rate.

**2. Complete a budget.** Add up all income and expenditure for the past year. If you haven't been keeping track of spending, make an estimate using your bank and credit card statements.

**3. Make a plan.** Using your budget estimate, work out how much income you have left each month to reduce your debts. If you have several credit cards and personal loans, concentrate on paying off the debt with the highest interest rate and highest balance first, and when that's repaid in full move onto the next highest. Look at the interest rate on your home loan, negotiate a lower rate with your lender or switch providers.

**4. Consolidate your debts.** You might also consider consolidating 'bad' debts into one account and shop around for the lowest interest rate. Use our office to assist if you wish.

Australia's household debt may be high by global standards, but that only becomes a problem if you are struggling to meet repayments or sinking good money into bad debts.

*If you would like to discuss a debt reduction strategy, don't hesitate to call.*

<sup>i</sup> <https://www.abc.net.au/news/2018-01-18/household-debt-extremely-elevated-and-tipped-to-grow/9340880>

<sup>ii</sup> Adelaide Bank/REIA Housing Affordability Report, December 2017 edition, released 6 March 2018.



# Learning to invest in yourself

Australia has had an extraordinary run of good economic times but the party is beginning to wind down with unemployment trending upwards and wages flatlining.

That's not an environment where anybody – young, old, self-employed or rusted-on staffer – can afford to coast. If you're not making the most of your capabilities, you might want to invest some time and energy in your most important asset – yourself.

Below, five respected life coaches suggest some life-changing, career-transforming techniques.

## 1) Work out what you want

If there is one thing successful people and organisations share it's clarity of purpose. High-performance specialist Phil Owens says, "Finding your purpose is like finding your personal true north; it gives direction to all of your decisions and actions. To find it he suggests asking: "What is important to me?" and "What do I love doing?"

"Be aware that everyone will have a different purpose and that working out exactly what yours is will probably be a much longer and more complicated process than you expect," he says

## 2) Act mindfully

Mindfulness is a concept that's crossed over from Eastern religion, particularly Buddhism, into the corporate world.

Satyam Veronica Chalmers, a trainer at Mindfulness Coaching, says mindfulness can translate into reduced anxiety, improved learning abilities, greater efficiency and improved concentration. Even better, practicing mindfulness is free and, once you get used to it, very easy.

"Stop periodically throughout the day for at least a minute to focus on your breathing, notice how you're feeling, notice bodily sensations and take some deep breaths. Set an alarm on your phone to remind yourself to do this," says Chalmers.

## 3) Polish up those soft skills

What separates the happy high-flyers from the not-so-happy plodders is often people skills rather than technical ones. Rhett Morris, human endurance expert and owner of Bulletproof People, says successful people are often high IQ but low EQ [emotional quotient]. By improving their EQ, they can get more out of people they deal with, whether that's employees, managers or their own friends and family.

Morris suggests taking a free online test, such as [www.ihhp.com/free-eq-quiz/](http://www.ihhp.com/free-eq-quiz/), followed by an 'emotional stocktake' to think about what impact your EQ has on those around you.

"Then begin holding yourself as accountable for who you are as what you do, both in the workplace and out of it," he says.

## 4) Link your goals

Linking your goals to something more motivating than a desire for personal advantage can also boost success.

Director of International Centre for Leadership Coaching, Alex Couley points out that humans became the most successful species on the planet by being cooperative. That means if we set goals with reference to how meeting them will improve the lot of others we'll be more motivated to reach them.

"For example, someone is more likely to work towards getting a pay rise if they're planning on using that money to send their child to a good school rather than just upgrading their car," says Couley

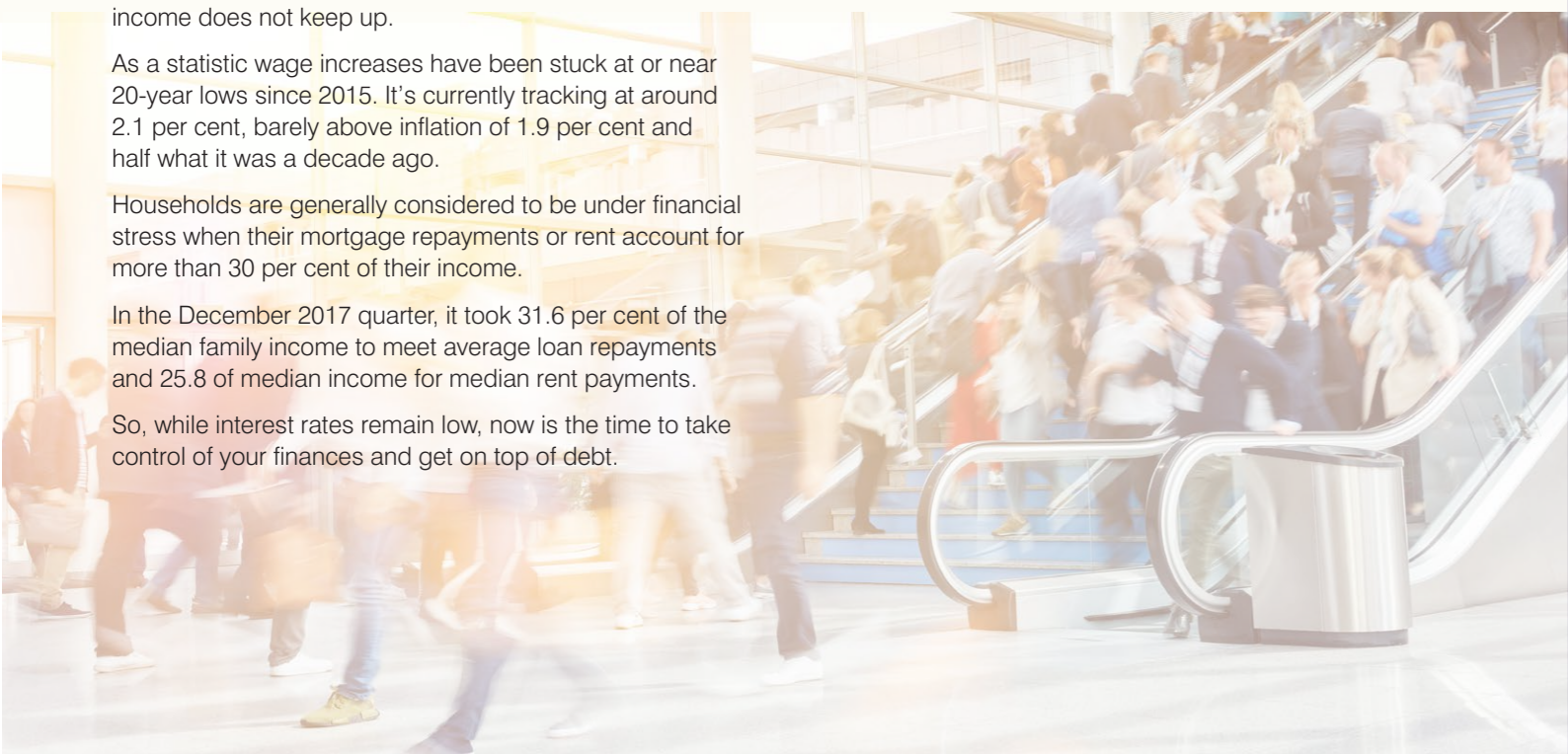
## 5) Investigate your money mindset

We're all at different stages of the wealth-creation journey, but if you feel as if your journey has stalled try doing a personal stocktake.

Money mindset coach Joanne Newell, of Rich Life by Design says that having your financial house in order involves the following: "You should have an income that reflects the value you provide or create, that income should be substantially more than your outgoings, you should have some quality investments and you should have a clear understanding of your financial position, which includes up-to-date bookkeeping."

If your finances are less than ideal, Couley suggests spending some time reflecting on any limiting beliefs you might have around money, including those inherited from your family.

None of these suggestions is costly or complicated but all have the potential to improve your career, finances and overall wellbeing. With the possibility of some challenging times on the horizon, there's never been a better time to invest in becoming more focused and effective.





# The Reward of Donations

The bushfire disasters across Australia over the past months have demonstrated the enormous generosity of Australians – from sporting stars, Hollywood heavyweights and business leaders through to ordinary people from across the country, all just wanting to help and make a difference. While the simple satisfaction from doing this can't be measured in dollars, with the right knowledge and planning aligned to your circumstances and objectives, there are also dollar rewards on offer for the giver come tax time.

## Taking philanthropy to the next level

Australians are generous when it comes to opening their wallet for a good cause. But you may have reached a point in life where you want to make a more substantial contribution with control over how your money is spent. You may also wish to get your children involved to instil shared values.

While it hasn't received much publicity, increasing numbers of Australians are using charitable trusts to give in a more planned and tax-effective way.

The turning point came in 2001, when the Howard Government introduced the Private Ancillary Fund (PAF) with the aim of encouraging more individual and corporate philanthropy. PAFs are charitable trusts that can be used by an individual or family for strategic long-term giving.

Since then, the number of PAFs and the amount of money contained in them has grown steadily. In early 2018, there were 1600 PAFs, housing \$10 billion and distributing \$500 million a year.<sup>i</sup>

## Claiming a tax benefit

According to Philanthropy Australia, in the 2015-2016 financial year 14.9 million Australians collectively donated \$12.5 billion to charities and not-for-profits (NFPs).<sup>ii</sup>

Though donations to accredited charities and not-for-profits are tax deductible, the figures indicate two-thirds of taxpayers don't bother to claim. It's well worth keeping track of receipts so you can claim when you think that, for example, a single donation of \$5000 to a charity or NFP in a financial year will reduce your taxable income by \$5000.

A core principle of tax-deductible philanthropy is that the giver shouldn't stand to receive any material benefit. For example, if you buy tickets in a raffle run by a charity you can't claim a tax deduction on the cost of the tickets. In order to receive a tax deduction for your donation, the recipient must also be registered as a **deductible gift recipient (DGR)**.

There are many ways to be charitable but the impact on your tax bill will vary depending on how you go about it.

## A more sophisticated approach

These days, people who want to take philanthropy to the next level with an ongoing, tax-effective approach have a variety of trusts to choose from.

### The Private Ancillary Fund.

PAFs are the best-known of the new breed of trusts. The money placed in a PAF is tax-deductible and assets in the fund aren't subject to income or capital gains tax (but do qualify for franking credits).

Let's say a dentist sets up a PAF and gifts half his \$500,000 annual income into the fund. The dentist's taxable income now drops to \$250,000. What's more, no tax is paid on the returns made on the \$250,000 that has been invested in the PAF. The dentist must distribute a minimum of five per cent of their PAF's net asset value annually, or a minimum of \$11,000. After meeting that requirement, the dentist has a relatively free hand about which charities to support and how much they receive.

### The Public Ancillary Fund (PuAF).

PuAFs work the same way as PAFs but operate on a larger scale. For example, 10 dentists may set up a PuAF to finance the building of dental hospitals in Africa. As well as gifting part of their incomes, the 10 dentists can (in fact, are obliged to) invite the general public to make tax-deductible donations to their PuAF.

### Testamentary Trust (or Will Trust).

These are used by individuals wanting to leave money in their will to charity. The two advantages of this type of trust are that the trustee(s) can distribute the income generated by the trust in a way that minimises the tax burden of beneficiaries, and the assets in the trust can't be accessed by parties such as creditors.

Few people give to get a tax deduction but by supporting good causes in a tax-effective manner you can achieve a bigger bang for your philanthropic buck. *If you would like to know more about tax-effective giving, give us a call.*

<sup>i</sup> J.B.Were Support Report, 4 April 2018, <https://www.strategicgrants.com.au/free-resources/blog/19-blog-kate/280-grantseeking-donor-giving>  
<sup>ii</sup> <http://www.philanthropy.org.au/tools-resources/fast-facts-and-stats/>





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Level 8, 525 Flinders Street Melbourne VIC 3000

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