MEDICAL AND DENTAL ACCOUNTING

THE HEALTH WEALTH SPECIALISTS

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INTRODUCTION

Welcome to the first edition of MADA News for 2008. We hope you've had a great start to the New Year.

We would like to extend a warm welcome to our newest staff member, Christine Armstrong who has joined us as our marketing and office manager. Christine will be well known to some of you as she was (until recently) the Project Officer for the Southcity Division of General Practice. We are very pleased to have Christine on board and she has already proven her worth as a valued member of staff.

And speaking of Divisions of General Practice; our year has kicked off to a great start with our latest presentation "What structure is right for you and the effect of various structures on asset protection and estate planning". We have again had very positive feedback to presentations already given on this topic and look forward to presenting this seminar to quite a few more Divisions before 30 June! This seminar is to be conducted by Ms Caroline Poon and run in conjunction with Ms Jo Dawson, our recommended financial planner from Hillross and a personal friend of Caroline's.

Watch this space too for another presentation specifically aimed at 58+ individuals. The Transition to Retirement Allocated Pension (TRAP) strategy is probably the most powerful wealth creation tool with zero investment risk to be introduced by the Federal Government in decades. We have organised to present to a number of Divisions on this topic and our presentation will look at:

- Working scenarios showing savings that have been achieved (and it is surprising how little you need in super to reap substantial tax benefits
- Steps to implement the TRAP
- Issues relating to the TRAP i.e. cash flow management, extra withdrawals, whether to use self managed superannuation funds or wrap accounts or a combination of the two

January and February have come and gone and now is the time to start preparing for year end tax planning!

Year end tax planning seeks to develop strategies to defer assessable income to the next financial year and bring forward deductions to the current year. In essence it should not be a mad scramble before year end; we should have put strategies in place throughout the year which facilitate the legitimate minimisation of tax and create wealth for you at the same time.

Each client's set of circumstances is unique and one size cannot fit all!

Please contact Christine to organize an appointment with me should you feel it is necessary to have a face to face meeting to discuss various tax strategies before 30 June 2008.

Meeting in person often brings to light issues that would not be readily addressed in a telephone conversation or via email. <u>This is particularly important for those clients who did not have a tax planning meeting with me prior to 30 June 2007.</u> Meetings may also be conducted before or after hours at mutually convenient times as I know that you all are (like me) a busy professional!

Caroline Poon
Director

Topic of the Month - Borrowing to invest through your superannuation fund

In our last newsletter we featured an article regarding borrowing to invest through your superannuation fund. There has been lots of press in relation to this in recent times and we thought it opportune to discuss this in more detail now.

Up until now there have been very few opportunities for funds to borrow directly (although they have been able to borrow indirectly via geared investment funds and listed and unlisted trusts and companies).

A superannuation fund can now borrow through a structure known as an ‘instalment warrant’. This is simply a way in which to gear/borrow on a limited recourse basis property or shares. A non recourse basis means that in the event of the superannuation fund defaulting on repayment of the loan, the lender only has the right to recover an amount up to the value of the investment that is subject to the loan. Instalment warrants are not a new invention and have been around with the large institutional banks for many years.

The borrowings can be made by a bank, related party or someone else.

The legislation provides the investment is held on trust for the superannuation fund so the superannuation fund has a beneficial entitlement to the investment. It has the right to acquire the ownership of the investment or its replacement.

The trust can be a bare trust or a unit trust and we like the idea of a bare trust. This means that the trustee simply holds the investment and transfers it to the beneficiary (the self managed superannuation fund) at the appropriate time. This is the most cost effective vehicle as the asset is simply shown in the balance sheet of the superannuation fund e.g. "Instalment Warrant (on property)" It should be noted that the trustee/s of the bare trust cannot be the same as the trustees of the superannuation fund. We recommend that if mum and dad are the trustees of the superannuation fund then just mum (or dad) can be the trustee of the bare trust.

Repayments are required to be made by the superannuation fund on an arms length and commercial basis (we would recommend monthly). When the last payment is made the investment is transferred to the superannuation fund.

If the superannuation fund defaults on the loan, the lender's right to recoup the amount outstanding is limited to the value of the property i.e. there is no access to other assets owned by the superannuation fund. For example a property is bought for $500,000 and the superannuation fund has borrowed $400,000 to purchase this. It is then sold for $350,000. The lender can only get $350,000 back and the loss of $50,000 will be borne by the lender.

The instalment warrant can invest in any asset that is allowable under SIS legislation e.g. commercial or industrial property, residential property and listed and unlisted shares.

Only one asset can be held in each trust for the superannuation fund. To this end we really only recommend property be held this way. If you have a large parcel of only one blue chip share, this is not spreading the risk or diversifying your investments!

What happens if the superannuation fund is unable to pay or does not continue to pay the loan?

The lender may force the sale of the asset to recoup the value up to the amount of the outstanding loan.

The legislation is yet to address refinancing.

<u>Which clients can benefit from this type of investment?</u>

1. Clients who are sole traders so cannot borrow to fund superannuation contributions and claim an interest deduction on the borrowings

2. Clients who are employed who can't get extra money into super by way of spouse employer contributions who wish to use gearing in superannuation but can't contribute

3. Clients around 40 or younger who wish to bring forward the purchase of property via superannuation earlier. By getting into the property market earlier, you accumulate unrealized capital gains and then sell the property at 60 tax free once you are in allocated pension mode.

4. Those that have reached the concessional ($100,000 for 50 and over or $50,000 for under 50's) or non concessional ($150,000 undeducted per annum or $450,000 undeducted prior to 65) caps. If you or a related party make a loan to your superannuation fund, your fund will not get caught up in penalties that apply if you have the potential to breach these caps.

Personally I still prefer the more direct ways of investment to more or less achieve the same effect.

1. Borrow to fund employer contributions to superannuation and get a tax deduction and buy the property outright in the superannuation fund

2. Buy a property as tenants in common between the individual and the superannuation with the security for the individual's borrowings on a property other than the one that will be part owned by the superannuation fund.

However these arrangements are not available to part of our client base e.g. employees, self employed (if borrowings are required to get contributions into super), etc.

Financial modeling is a must to prove that this type of investment adds value to your overall wealth strategies. Product providers are starting to emerge and it will be interesting to see interest rates on these loans, lending to valuation ratios (predicted to be between 40 to 70%). We would envisage that personal guarantees will be required also.

<u>We will be organizing some informal seminars in relation to this particular topic using working scenarios based on actual client circumstances (with the identity of the client/s disguised of course). Further information will be advised once we know what the banks/financial institutions are offering regarding lending on instalment warrants.</u>

The contents of this newsletter are general in nature and are not advice that applies to any particular client situation. Whilst every care has been taken in preparing the newsletter, specific advice should be obtained before proceeding with any suggestion or recommendation made in this newsletter.