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Welcome to our April 2011 issue of our 'Horsey Jameson Bird Newsletter'.

The purpose of this newsletter is to keep you informed of developments in financial planning and taxation services. We aim to keep you up-to-date on relevant industry and regulatory changes as well as advising you of the services provided by Horsey Jameson Bird (HJB).

Message from Di



Events over the past two months have reinforced why we prefer the Australian sharemarket over global sharemarkets.

We have witnessed the devastation of the Queensland floods and cyclone in January, the Christchurch Earthquake in February and the Earthquakes and Tsunami in Japan in March, all resulting in an enormous loss of life and property. The impact of the Japan earthquakes, tsunami and nuclear issues are expected to lead to, not only a significant rebuilding of the affected areas, but also a revision of appropriate material for such an earthquake prone nation. Japan is expected to draw on its vast sums of surplus capital which has been invested overseas to fund the rebuild. We expect that Japan may refuel its energy requirements with liquid natural gas rather than uranium fuel rods which is positive for Australia.

The US continues to artificially lower the cost of capital through policies such as quantitative easing and cheap interest rates. These policies are concerning, as cheap money lead to excessive risk taking just before the Global Financial Crisis. To move the federal deficit into surplus and to start repaying debt is the biggest challenge facing the Political Parties in the US. Our exchange rate with the US confirms that the Market shares our concern with the state of US debt. These universal concerns are evident with our dollar buying 109 US cents recently.

Locally the Commonwealth Budget for 2011-12 will be announced on May 10. We're expecting a tight budget. The Government has indicated a preference to return to surplus within two years. We expect that the usual suspects – welfare reform, defence and family benefits – will be discussed. It will be interesting to observe whether the current 50% reduction in minimum pension payments will be extended.

Paying off the mortgage or maximising concessional contributions to super

Clients who have borrowed to purchase their principal home may be inclined to direct any surplus income to reducing the size of their mortgage and becoming debt free as soon as possible. But is this always the best course of action?

Analysis suggests that for many clients, a superannuation concessional contribution strategy over a fixed period of time can provide an improved outcome with the end result being reduced debt and a higher super balance to fund retirement income.

This alternative strategy will be best suited to clients who:

- Have a marginal tax rate (MTR) of 30% or higher
- Will retire after reaching age 60 and are within 10-15 years of retirement
- Will not breach their concessional contributions cap when any additional concessional contributions are made.

The following example highlights the relative benefits that a concessional contribution strategy can provide.

Terry and Pam

Terry and Pam (married) are both age 50. They are employees with a MTR of 31.5% (including Medicare Levy) and are not currently making any voluntary super contributions.

Terry and Pam have recently purchased a new home. Their mortgage of \$400,000 requires them to make minimum mortgage payments of \$33,868 pa (\$30,000 interest, \$3,868 principal). The current variable interest rate on this mortgage is 7.5%.

Due to recent salary increases, extinguishing a personal loan and setting a new budget, Terry and Pam have found an additional \$18,000 pa in after tax income to invest. They can elect to increase their mortgage repayments by this amount, or they could instead each elect to make concessional contributions to super via salary sacrifice (\$26,277 combined) to the point that they eliminate their surplus income.

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HJB Staff Spotlight - Russell Phillips

Russell Phillips joined HJB in January 2011 as a Certified Financial Planner to assist in providing financial planning services to HJB Clients. Russell has worked in the financial planning industry for 15 years in a variety of roles. He specialises in providing assistance and advice to clients with complex needs, helping them grow their portfolios.

Russell moved from Melbourne to Brisbane in 2002 to live with his soon-to-be wife, and now has two young daughters attending primary school and preschool. Russell attended the selective entry Melbourne High School, and excelled academically, twice finishing in the top 0.3% of students nationally in the Australian Mathematics Competition. After graduating from Monash University in 1995 with a Bachelor of Commerce

degree, Russell commenced employment with a small financial planning practice, moving into the position of financial adviser by his mid-twenties. Russell also completed a Graduate Diploma in Financial Planning from the Securities Institute during this time.

Russell subsequently worked for a major bank specialising in formulating and writing advice for Private Bank Clients with diverse requirements. Upon moving to Brisbane, he concentrated on training Financial Advisers on devising strategies to improve the quality of their advice. Russell's most recent professional role prior to commencing with HJB was as a technical specialist, with high net worth national financial services firm. Russell is a member of the Financial Planning Association as a Certified Financial Planner.

Client Taxation Services Manager Profile – Gina Patrick

Gina Patrick joined HJB in 2010 as Client Taxation Manager and part of the HJB leadership team. Gina has been in the business, accounting and tax advisory field for over 25 years. She is a Certified Practising Accountant, a Fellow Member of CPA Australia and a Registered Tax Agent.



Prior to returning to Brisbane, Gina enjoyed a broad and successful career in the Mackay and Whitsundays region in various industries. In 1995 Gina founded and successfully operated a CPA Public Accounting and Tax Consultancy Practice until in 2002, when she decided to sell her practice. Whilst in practice, her client base was predominantly small to medium enterprises in a variety of industries including property development, cattle grazing and sugar cane farming, heavy industry, retail and various service industries.

Gina went on to senior finance roles in various industries including Financial Controller in the banking, manufacturing and tourism industries and a period as Acting General Manager of Tourism Whitsundays.

Gina was the North Queensland finalist for the young CPA of the year award in 2001, an award designed to recognise excellence in accounting among CPA members under 35. In 2004 Gina joined as a member of the Australian Institute of Company Directors and graduated from the AICD Company Directors course in the same year.

Having experience with the breadth of clientele and industry enhances Gina's ability to assist and service business owners and individuals alike to increase their business performance and minimise taxation. She has long standing associations with her clients and believes in the mutual benefits that can be gained by having an Accountant who understands your business and the way you operate.

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Outcome

After one year, Terry and Pam's situation is as follows:

	Reduce mortgage	Concessional contributions
Combined mortgage	(\$378,132)	(\$396,132)
Combined superannuation ¹	Nil	\$22,336
Net wealth	(\$378,132)	(\$373,796)
Benefit		\$4,336

After 10 years, the benefit is significantly increased as shown below:

	Reduce mortgage	Concessional contributions
Combined mortgage	(\$90,624)	(\$345,272)
Combined superannuation ²	Nil	\$302,048
Net wealth	(\$90,624)	(\$43,224)
Benefit		\$47,400

1 For comparison purposes Terry and Pam are assumed to have no other superannuation. Accumulated superannuation is assumed to earn 7.7% pa, all taxable at 15%.

2 If under 50 years of age at the end of the financial year, the concessional cap is \$25,000.

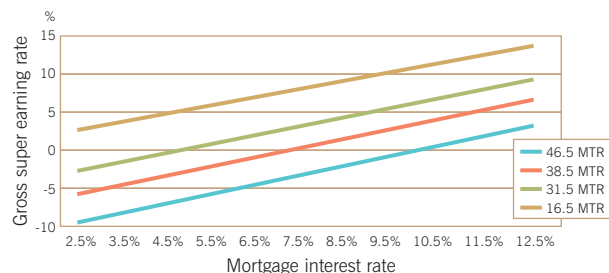
Analysis

Using surplus income to make additional mortgage repayments is a sound strategy for Terry and Pam. They are able to generate more wealth over 10 years by continuing to make minimum mortgage repayments and implementing a concessional contribution strategy. Once aged 60 and retired, they can then withdraw a tax-free lump sum from their superannuation balance to reduce their mortgage to around \$43,000.

For Terry and Pam, the key driver behind the benefit of their salary sacrifice strategy is the difference in the value of ongoing capital injections throughout the timeframe. By repaying their mortgage as quickly as possible, they are able to pay off an amount equal to their after tax income surplus (only \$18,000 pa). However, salary sacrificing from pre-tax salary allows them to make gross contributions of \$26,277 combined, or \$22,336 after 15% contributions tax.

Increasing interest rates and reduced earning rates

Both the mortgage interest rate and earning rate within super are important variables in any comparison between reducing debt and making concessional super contributions. It is therefore important to analyse how the outcome would change if the mortgage interest rate and/or the earning rate within super changed. Graph 1 shows the earning rate required within super for Terry and Pam to at least break even by implementing a concessional contribution strategy instead of reducing their mortgage, for a given range of mortgage interest rates. We have also highlighted how this required earning rate would change if Terry and Pam's MTR increased or decreased.



We can see that Terry and Pam can still benefit to some degree from the concessional contribution strategy if earnings within the super were as low as 4% pa. This is because regardless of the earning rate, a key driver of the strategy (the higher ongoing contribution throughout the timeframe) remains in place. In the same way, if earnings were to remain at 7.8% pa, an increase in interest rates to around 10.5% will still leave Terry and Pam better off implementing the concessional contribution strategy.

It is also apparent that the concessional contribution strategy is more likely to be beneficial for those on a higher MTR (subject to any contributions not breaching the concessional contributions cap). For example, if Terry and Pam had a MTR of 46.5% and their mortgage interest rate was 7.5% pa, they would still benefit from the concessional contribution strategy if their superannuation experienced nil earnings.

Please note that the advice above is general in nature, and may not apply to your circumstances. Please seek our advice if you believe that you may benefit from the strategy of higher super contributions, as the most appropriate strategy for you may differ from the strategy outlined above.