Goodman & Co.

NEWSLETTER

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NEWSLETTER

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This planner is written to assist in recognising issues and implementing strategies prior to year end to maximise profits and minimise taxes payable.

Increasing your personal wealth and reducing your taxes is what strategic planning is all about.

Taxes, superannuation, dividends, equities and properties all need to be considered as they are all (including taxes) an integral part of your Family's Wealth Creation Strategy. If the strategy is to work, all of the elements must be considered and kept in balance. Planning for the above topics is all part of the Family Strategic Plan.

You need to have a Wealth Creation Strategy that deals with lowering tax rates across the income spectrum, increases the return on investment and frees up cash that would otherwise be paid to the Australian Taxation Office.

For additional copies of this Newsletter please contact our office on +612 9232 1588 or visit *www.goodco.com.au*.

OVERVIEW

This Newsletter is fairly technical but covers day to day matters of which Parents, minors, young adults and others should be aware of.

Parents have Children and when those Children come of age they may meet a partner and possibly live with them, get married, buy cars, homes and acquire investments. There are many tax and asset protection issues which arise and seem to get lost in the passing of time. Knowledge and asset protection are often not passed on from Parent to Child.

This Newsletter attempts to cover strategies which Parents should have in place from a very early age for their Child to assist the Family in formulating and implementing Savings, Family Wealth Creation and Asset Protection strategies.

Hopefully by the time your Children reach retirement, they will have secured a financial base to afford a very comfortable life for themselves and their Partner. In addition, you would hope your Children would be in a position to provide their Children with some financial assistance for schooling, university, holidays and other life events, such as Engagement and Wedding costs should they desire to do so.

Children should **NEVER** be given money to assist them with the purchase of a house etc. This should **ALWAYS** be by way of a formally documented, legally binding, **LOAN** drawn up by a Lawyer. If you want to protect the Assets for your Children, it will be well worth the cost of having this documentation legally prepared and executed, ensuring you follow the rules. Failure to observe formalities can be catastrophic as so many have found when their arrangements are tested before the Courts. The worst case scenario may be the Courts dismissing the arrangements as a Family sham, resulting in the loan being set aside.

Loan Agreements, Mortgages (preferably registered) and periodic Loan Statements should be prepared, especially when you are dealing with Family members. Failing to have these documents may put the loan at risk, especially if the arrangement is attacked by a third party or in Court.

As your Children grow, it is wise to teach them how to save, especially by the time they become teenagers. It never ceases to amaze us at how many young people have absolutely no idea how to save.

The simple strategy of putting aside a little money each week or month can lead to a tidy sum in the future.

The by-gone era strategy of accumulating savings in a fee-free, interest bearing account and then buying Blue Chip Investments a little at a time seems lost on the younger generations coming through. For those Children who have missed this important lesson, when this is demonstrated to them, especially how Compound Interest over time creates wealth as a very simple example, we are usually asked “Why did someone not show us this years ago?”

In addition to teaching your Children how to save from a young age, you can assist them in developing and advancing their savings strategy as they grow through gifts. Such gifting can include giving your Children a Discretionary Trust as their 21st birthday present.

These savings may create wealth sufficient to put towards deposits on homes, overseas trips, marriages and honeymoons etc. and in particular will get you or your Children into a savings and wealth accumulation habit.

Saving should start at an early age. It is a sobering reminder to us all that many independently wealthy people will tell you that their Wealth Creation Strategy started from their Parents, who insisted that they put money aside from their own efforts and / or from small gifts from family and friends. This simple, timeless Investment Strategy, implemented and developed over a lifetime sees them as independent and financially secure.

Many would suggest that the ultimate Investment Strategy is achieved through Superannuation. Superannuation should always be part of any person's Investment Strategy but should not be "*The Strategy*". When considering Superannuation, factors such as contingent taxes and hidden costs, need to be taken into account as these can erode your savings over time. Some hidden traps in Superannuation are mentioned later in this Newsletter.

Using the right Structures and Wealth Creation Strategies can yield tax savings.

Initially, when we started writing this Newsletter we thought it would all fit into one Newsletter. As we progressed, we realised how many issues are faced by Parents and Children as they proceed through life, and therefore we will be addressing these issues across the next few Newsletters, such as Separation, Divorce and Death and the Income and Capital Gains Tax (CGT) consequences of those events.

This Newsletter has been written for you, however as it is a fairly heavy subject and so to lighten it up we have written it to your Children.

HATCHES – PREPARING FOR THE FUTURE

Regardless of whether your Parents are wealthy or not, sadly you will produce minimal financial advantages for your Parents. You are going to cost them a lot of money, so hopefully you will give loads of love and affection in return.

Until you turn eighteen, depending on what income you earn, you may be taxed at the top marginal rate – which is currently 49% - from the first $1.00 since the Former Federal Government removed the tax benefits previously available to minors (people under the age of 18 years).

When you are eighteen years old, your Parents may seek advice and try and access your non-tax or low-tax status on income. For example in the current year, if you have a part-time job earning you pocket money you can earn $18,200 before you pay any tax. After that you will be paying tax at the rate of 21% until you earn $37,000 at which point the tax rate is 34.5%.

This will be very attractive to your Parents because they will be paying tax at the top marginal rate (currently 49%). They will suggest to you that you've been distributed income from the Family Trust to help build the Family Wealth by saving the Family money through accessing your lower tax rates.

This will more than likely continue until you are someway through University. You may find that while studying and working part-time, you no longer get a refund cheque from the Tax Office. This may be in part because of the additional income distributed to you by your Parents pushes your tax payable up and puts you over the HECS debt repayment threshold (FEE-HELP and / or

HECS-HELP). If your Parents are smart, they will pay you the additional amount of tax so that you stay in the same after-tax position.

The fact that you're saving the Family substantial amounts of tax will not appease you:

- You will want a tax refund;
- You will want to delay your HECS debt repayments until you are earning sufficient income; and
- You will want to be independent.

In total frustration, your Parents may stop distributing income to you and withdraw your financial assistance. You will then be accountable for your own earnings and taxes, as well as savings plan.

Your Parents are hopefully aware by this stage that many of your contemporaries who have reached adulthood have discovered they have accumulated a substantial loan owing to them in their Family Trust. These loans are the accumulated distributions that they have received over many years.

Sadly, some Parents and their Advisors will net off the distributions made to you when you were younger against your Parents' Allocated Funds accounts so they don't have to show a loan. Unfortunately this can be undone if challenged in Court: often it is argued that such netting off is not legal, with further claims that the money has not been spent for your benefit. This can put the Trustee(s) in hot water. The good news for you is that you'll most likely win, or if you are in the Family Court later in life, your Partner will likely win.

If history can teach us anything, it is that a fair number of you, possibly more than you would believe, will ask your Parents for repayment of these amounts or go to the Courts and sue your Parents to recover these amounts.

Often these loans are discovered when you are in adversarial proceedings with your Partner who is claiming that these amounts form part of the Joint Assets. Sadly, your Partner is likely to be successful in this claim. This scenario is played out on a daily basis in the Courts with you and your Parents saying to Accountants and Lawyers "Why didn't someone tell me?"

Through good Family Tax Planning, you and your Parents may be able to protect yourselves against claims by your Partners by ensuring you are not owed any amounts from the Family Trust. This can be achieved by you telling your Parents early on that they need to set up a loan account in the Trust. From this loan account they should then pay all your pre-schooling, education and holiday expenses.

We **DO NOT** ever recommend that your Parents' Trust distribute to your Partners or their Children because it may create a future claim against the Family Trust. This could compromise the Assets your Family is trying to protect. Distributions should only go to immediate Family Members, a Trust or Corporate entity controlled by the Family. If Distributions are to be made to your Partner or Children then you should setup a separate Discretionary Trust for them and the Distribution from the Parents' Trust should be made to that Trust.

If you set up a Trust then ideally: your Parents should not hold any Office in the Corporate Trustee; you should be the sole Officeholder (Director and Secretary); and be the Appointor of the Trust.

Testamentary Trusts

After you are born hopefully your Parents will change their Will to either appoint Guardians for you and Executors or Managers to control the Family Wealth (if both Parents do not survive).

The structure usually recommended to your Parents should both of them die (and only while you are in pre-teen years) may be a Testamentary Trust. This is a Trust created by their Wills which is settled (or comes into existence) on death. This should provide financial security for you in the event of both their deaths. It should cover your childhood, perhaps your University years, up to and age when your Parents believe you are mature enough to handle your own financial affairs.

The earliest you can access the Trust Funds (Capital) will be the date set by your Parents in the Testamentary Trust Deed (which is known as the Vesting Date) or if not set, when you legally become an adult (i.e. eighteen years old). Although you are restricted from accessing the Capital of the Trust, the Trustees can access the Trust Funds to pay for your care and education.

Careful consideration needs to be given by your Parents when selecting the Vesting Date. Whilst it is not uncommon for them to select the Vesting Date until you are middle-aged, this can have adverse tax consequences and bars you access to the Capital when you may need it most. This may also unintentionally erode the Family's Wealth.

Whilst you are a minor, the income distributed to you by the Testamentary Trust is assessed in the hands of the Trustee as though you were an adult using marginal tax rates. The current adult tax rates of:

The first	$18,200	is tax free,
The next	$18,800	is taxed at 21% (plus 2% on the first $18,200)
The next	$43,000	is taxed at 34.5%
The next	$100,000	is taxed at 39%
And	any excess	is taxed at 49%

Normally, minors are taxed at the rate of 49% on all non-exertion income, so there are tax savings in using this structure. If that income was distributed to you by a Discretionary Trust while you are under 18 years of age then you would be taxed on **ALL** the income at the rate of 49%.

This all seems wonderful, however a Testamentary Trust is an expensive structure to manage and administer, as well as inflexible. Therefore as you approach adulthood, your Parents should consider other options to maximise the Family Wealth for you and your siblings, which provides flexibility, minimises the costs of administration and considers your possible future financial positions. Tax consequences, such as Capital Gains Tax and the ability to Tax Plan, should also be considered and advice sought in this regard.

If your Parents set up a Testamentary Trust, particularly in your formative years, then such Trusts should ideally Vest when you and your siblings are no older than twenty-five to thirty years of age. It is strongly recommended that the Trustee be a Corporate Trustee which is established at the time the Wills are executed. Your Parents can control these Companies initially by appointing themselves as Stakeholders and Directors.

Your Parents should review their Wills and the appropriateness of this structure as theirs, yours and your Siblings' circumstances change, such as becoming an adult or entering a permanent relationship with a Partner.

Discretionary Trusts

As you become a teenager, you are hoping if your Parents created Testamentary Trusts in their Wills when you and your Siblings were younger, that someone will have reminded them that it may be time to revisit and update their Wills.

Ideally, your Parents will have created, implemented and be maintaining a Wealth Creation Strategy that may include the use of a Family Discretionary Trust ('Family Trust'). A Family Trust (as distinct from a Testamentary Trust) is often used for accumulating Assets, Asset Protection, Family Tax Planning and passing wealth between generations.

If your Parents use a Family Trust as part of their Will, ideally both the Will and the Family Trust Deed should be written at the same time to achieve the same outcome. Sadly, this rarely happens in practice.

Your Parents should avoid accumulating Assets in their own names, except for the family home, by investing through a Family Trust. They will no doubt control the Trustee and therefore control the Assets and operations of the Family Trust, including how income and gains are distributed. This discretion is the distinguishing feature of this type of Trust.

The Trustee may distribute income and / or gains to Beneficiaries, who are defined in the Family Trust Deed when it is set up and usually includes your:

- Grandparents;
- Parents;
- Aunts and Uncles;
- Children;
- Grandchildren;
- The Spouses of the above; and
- Any Company or Trust which any person above have an interest.

Despite this, it is important to note that no-one has a right to income and / or gains, either in a particular year or in every year, even if they have received distributions in the past. Further, no beneficiary has an enforceable right other than to receive what is distributed to them previously and *to be considered* for a distribution.

This makes the Family Trust the Rolls Royce of Family Tax Planning as it is: relatively cheap to set up; extremely flexible; and a product that suits most wealthy and not so wealthy clients. It is also the perfect vehicle for retirement savings as it can still be used throughout retirement for Wealth Maintenance and Tax Planning.

Sadly, these advantages are rarely explained to your Parents or realised. Although the Family Trust may provide the Family some benefits, the Tax Planning opportunities are not maximised either because no Tax Planning is done, or it is done after year end, or advice is sought from professionals that do not have specialist Trust knowledge. To maximise the benefits from this structure, your Parents should seek advice from and work collaboratively with established, reputable professionals in this area.

When it comes to effective Tax Planning:

- *if not done well before year end, it is usually ineffective and minimal;*
- *if done efficiently, the benefits will far outweigh the cost of the plan; and*
- *if the savings are unclear, then don't do it!*

When used correctly, the Family Trust can defer the Capital Gains Tax consequences associated with your Parents death, as well as minimising costs of dealing with their Estates. Your Parents may use a similar strategy to postpone the payment of taxes which allows the Family to invest the delayed taxes to further grow the Family Wealth.

Similar to Testamentary Trust, the Family Trust has a Vesting Date which is set by your Parents. This may be either after eighty years or at a time determined by your Parents. It is not uncommon to find clauses written into the Deed which Vest the Family Trust to you and your Siblings once a set period (say five years) after the death of the last of your Parents has expired. This gives you and your Siblings time to work out what you want to do and Vest the Family Trust's Assets. ***Hopefully, your Parents will not want to rule your lives from the grave***.

The beauty of the Family Trust is that your Parents are giving very valuable Asset that has the gift of flexibility. Essentially, you and your Siblings receive a vehicle that can distribute your inheritances to yourselves and / or others of your choosing, without creating Stamp Duty and Capital Gains Tax consequences. In other circumstances, the death of your Parents or on the Vesting of your Testamentary Trust, tax consequences would be triggered.

Keeping or withdrawing from the Family Trust will very much depend on you and your Siblings' individual financial circumstances at the time, as well as your ability to cooperate to run the Family Trust. For those wishing to access their Capital, they can be paid out with minimal CGT consequences to the Family whilst those who elect to continue with the Family Trust do not suffer any CGT consequences of other siblings having different financial needs.

These are tailor-made structures and, if thought through properly, should deal with anything your Parents may want to happen on their death. Your Parents may want the Family Trust to Vest upon their death. Alternatively, they may want the Trust to continue so it can distribute to you, your Siblings, your Children and / or your Siblings' Children as though it is part of their Will.

They may exclude you and your Siblings from accessing the Capital because your Parents don't see the value in leaving their Wealth to you. They may in fact Vest the Trust Capital on their deaths to a charity or charities by bequest and only provide you and your Siblings with the proceeds of the sale of their home. Such bequests are more commonplace today and your Parents should ensure that certain steps are taken so their bequests can withstand possible legal challenges by you and your Siblings. Whilst gifting to charities may seem harsh, often Parents want to see their Children and their Children's Partners independently successful and not sitting around waiting for their Parents to pass on their Wealth.

So now that you know, what should you do?

> You should talk to your Parents and insist they see a really good Tax Lawyer or Tax Accountant - someone that really knows their stuff when it comes to Discretionary Family Trusts and Wills. You want to remind your Parents that their Wills and Discretionary Trust Deed should capture their intentions, especially regarding their Estate Planning for you and your Siblings**.**

*Off the shelf Trusts purchased from Incorporators, Lawyers or Accountants should be avoided at all costs. They are usually very badly drafted, inflexible and are a generic answer to everyone's problems. The old story applies – **you get what you pay for in life**. Cheap start-ups are often found to be very expensive in later years.*

MATCHES

At some point, likely in your 20's, you are or will be thinking about getting into a relationship. You have probably been to University and have commenced employment as a graduate in an industry of your choice. You won't be on a great salary but you will be saving for overseas holidays, cars etc. Further, someone will have had "that" discussion with you about it being time to "settle down"….

By this age, you hopefully have an established savings pattern and a few thousand dollars put away for a rainy day. If you don't, this is the time to start saving. Over the next five to seven years you are probably going to get married and want to pay for that wedding rather than have your Parents pay for it. You will of course expect your Parents to contribute towards it but being the age you are, you won't want to be told what to do – like inviting those thrice removed cousins you've never met but have to attend your wedding.

At some point in time you are going to meet your Partner and to the horror of your Parents you are going to move in together. The last thing you want is someone telling you that you should have a **Cohabitation Agreement,** but the reality is that if you're sharing accommodation for more than three months and your relationship breaks down, one of the parties could sue the other as though you had been married. If your Partner walks because you've asked for a Cohabitation Agreement, then that's more than likely telling you something.

Many professionals will tell you clients have said *"we just moved in together… we just started a relationship … we discussed if we broke up and agreed we both would pack our bags, take what was ours and move on…."* Unfortunately, breakups rarely play out this way – it is more likely that your Partner sues you for part of your Wealth, including Assets given to you by your Family. Sadly, to make this go away you are going to have to pay something unless you have a Cohabitation Agreement.

When you meet your future Spouse the same applies. Hopefully prior to getting engaged- and definitely before the marriage- you both have the maturity to go and talk to a Lawyer that specialises in **Prenuptial Agreements**. This is not something your corner-shop Lawyer can do for you. Both this and the Cohabitation Agreement needs to be written by a Lawyer and they are going to cost you a couple of thousand dollars each. At the same time, you should consider getting your Will done, as your current **Will will be null and void at the time of marriage**.

You will say "this is ridiculous" but consider this: what happens if your relationship breaks down and you have created substantial Wealth, your Parents have given you some Assets and / or you have inherited under your Parents' Wills? You will find that your Partner will make claim to part of all your Assets. If your marriage dissolves for any reason - even after your kids have left the nest - then you will wish you had. With a Prenuptial Agreement you can deal with your and your Spouse's current Wealth as well as potential inheritances.

Ideally you should revise your Wealth Creation Strategy and structure when drafting a Cohabitation or Prenuptial Agreement to ensure it can withstand attacks from third parties.

Many Shareholders, Partnership or Prenuptial Agreements have saved the parties because they have pulled out the Agreement and realised that the financial consequences of severing the relationship. If sufficiently onerous, the others realise it is better to sit down and try and resolve the issue rather than leap into protracted and very expensive Proceedings. They are also emotionally draining.

If an Agreement is not in place, the Family Court may suggest that as the Assets are now part of the Family Wealth they form part of the asset pool that needs to be divided in the Family Law Proceedings.

When you get married, Assets are usually pooled to facilitate your Family Wealth Creation and Tax Planning Strategy. You and your Spouse will try to accumulate sufficient funds to acquire a family home, perhaps a place in which you can have and bring up your Children.

Let's deal with some of the bigger issues of marriage as it relates to assets.

Let us suggest that you and your intended Spouse are about 28 and 32 years of age, both of you have moderate savings and investments and you both own your own domestic residences and have large mortgages over those residences. It is your intention to get married and either move into one of the homes or rent or sell one or both of the residences and buy a new home.

For Capital Gains Tax (CGT) purposes your domestic residence will be CGT free if it has been used exclusively as your domestic residence. For any period it has been used for work or rented it is not your domestic residence. The proportion of the gain that relates to this work or rental period will need to be included as your Taxable Capital Gain.

Many people believe their home is their castle and is CGT free but this is not always the case. Like any other asset, you should keep a Register of what you pay for the Asset, Stamp Duty and legal costs. If you renovate your home at some point, you should document these improvements in your Main Residence Property Register so that in the future if part of the gain is subject to CGT you will know what the cost base was. With that understanding, one or both of the houses may become subject to CGT.

Therefore it's important that if you don't already have a Property Register, you create one that includes all costs spent on your residence. When the time comes to sell your property, you should seek the advice of a Tax Accountant as to the tax consequences (if any) of the Sale. Likewise, you should seek advice from your Tax Accountant before purchasing any Asset to ensure it achieves your Wealth Creation Strategy.

You and your Spouse should seek the advice of a reputable Tax Accountant to develop your Family Wealth Creation Strategy, Tax Planning Strategy and to address the various tax issues that arise from and during marriage.

SEPARATION AND DISSOLUTION OF A RELATIONSHIP AND DISPATCHES

Are very big subjects and will be dealt with in future Newsletters.

SUPERANNUATION

The following is relevant and applicable:

- The maximum concessional contributions that can be made in the year 2015 is $30,000 except where the Taxpayer was aged 49 years or over the maximum for the year 2015 is $35,000.
- Retirees over 60 years of age with Superannuation benefits from a taxed source can have that superannuation paid to them tax-free either in a lump sum or by way of a pension.
- Taxpayers can make non-deductible contributions of $180,000 per year for 2014 / 2015 year, or $540,000 over any three year period where the Taxpayer is less than 65 years of age.
- The Superannuation Guarantee Rate is 9.50%. The rate will then remain at this level until 30 June 2018 at which time it will increase by 0.5% each year until it reaches 12% in 2022 / 2023.

Things you should ask your Superannuation Adviser and / or check:

It may be worth asking your Superannuation Advisor, if they converted your superannuation to a pension for life, how much would you get before and after tax in your hands?

You should also ask "if I die, is there any tax on my superannuation in the hands of the Fund in realising the Assets to pay out my nominated Beneficiary? What are the tax consequences of the death payout in the hands of my nominated Beneficiary?"

You should also check your Will and your Superannuation Nomination type to see if death benefits form part of your Estate or go directly to your nominated Beneficiary.

The things you should be very aware of:

For Self-Managed Superannuation Funds - The Trustees of your Superannuation Fund should be a Corporate Trustee i.e. a Company in which the Shareholders and Directors are the Members.

If you are in "Pension mode" or "on a Transition to Retirement Pension" then the earnings of your investments in your pension account are tax free. ***HOWEVER*** *depending on the terms of the Pension it is more than likely on your death they revert to "Accumulation Mode" and then all Income and Capital Gains derived in liquidating the Fund to pay out your Entitlement will be subject to tax.*

If your Beneficiary is not a dependant, a further tax will apply to the Beneficiary at about 15.00% plus Medicare Levy. This works like a de-facto death duty but is rarely brought to a Members attention by their Advisers when Superannuation Funds are being considered as part of the Family Investment Strategy.

If someone is terminally ill or close to passing on, then it is strongly advisable to obtain Tax Advice to maximise the passing of Assets to their intended Beneficiaries.

WILLS

In a letter to Private Clients in February 2014, the National Australia Bank provided the following statistics:

- One in six individuals either have no Will or are relying on a "Will Kit" Will.
- More than half incorrectly **believe life insurance and superannuation are automatically included in their Will.**
- 48% have no measures in place to protect Beneficiaries.
- 86% expect their Spouse or Partner will make medical, legal, financial and lifestyle decisions if they become incapacitated, but 40% of them have no documents in place to ensure this occurs.

It's a timely reminder as part of your Family Protection Strategies to ensure you have the documents listed below in place. These should be reviewed and updated when your circumstances change, or at least every five to seven years.

The documents you should consider having are:

1. **A Will** directs your Executors on how to administer your Estate, the location of which should be known to your Executors.

2. **A Memorandum of Wishes** indicates to your Executors what you are trying to achieve, what you do not want to happen, etc.

   This is not a legally binding document and is typically used to explain the reasons for what you have incorporated into the Will. This is because there are many instances where the Will cannot be located by the Executors even though they know it exists.

   In our opinion, this would be more effective because it is clearly then an integral part of the Will and evidentially may be used to ascertain the wishes of the writer.

3. **An Enduring Power of Attorney** gives directions to your loved ones should something happen rendering you incapable of making decisions for yourself. This document gives your Attorney an understanding of your wishes and it is enforceable.

   An ordinary Power of Attorney has limited effect and only operates whilst you are capable of giving instructions, but not in the same geographical location where a document may need to be executed.

   An Enduring Power of Attorney works irrespective of whether or not you are capable of giving instructions.

4. **An Enduring Guardianship** provides your Guardian with the power to make personal decisions for you, both financially and medically.

   Typically without a health care directive, the Enduring Guardian would be reluctant to make possible life ending decisions. Decisions they would make would include having you moved to a nursing home, put under full-time care, etc.

5. **A Health Care Directive** instructs the person holding your Enduring Guardianship what to do in a medical situation where that person may be loath to make some hard decisions in regard to your ongoing medical support. This document is not enforceable, but is akin to a Memorandum of Wishes.

You should discuss with your Solicitor and Accountant the merits of having the above documents. These should be prepared by a Lawyer, ideally the original documents should be held in fireproof storage with a second set of originals held in an alternative location in sealed envelopes.

