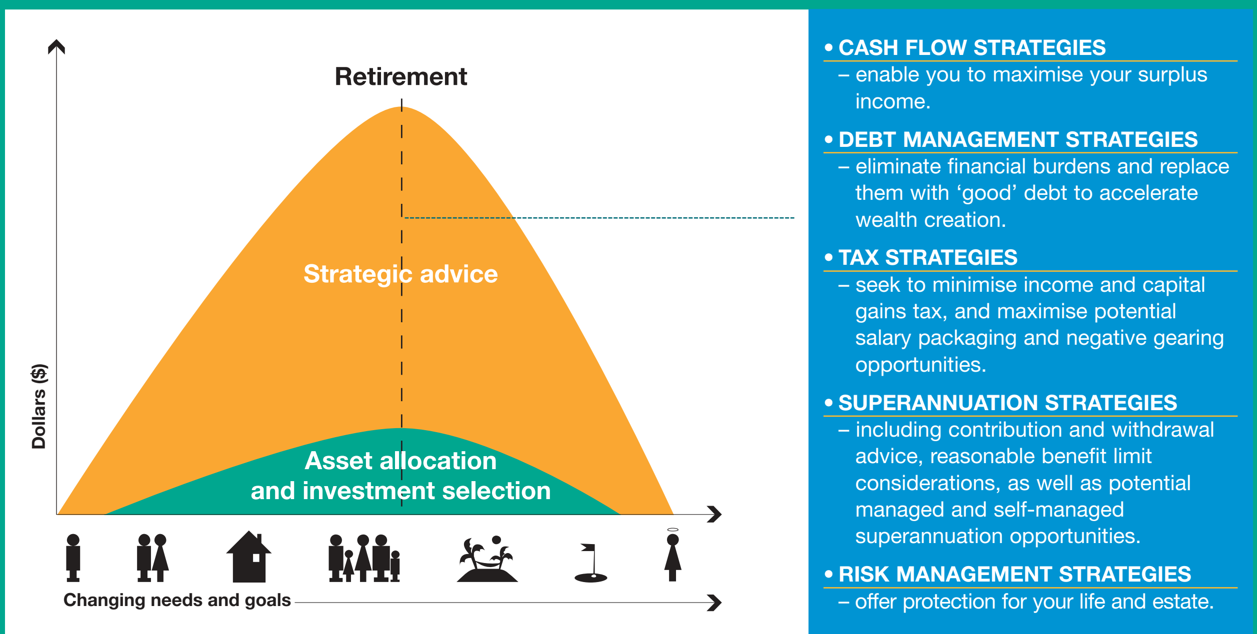
THE VALUE OF ADVICE FOR

baby boomers

When your children's wedding photos are replacing their baby photos, and a noisy household seems a distant memory, you could well find yourself in two minds. You look back on the rewarding (sometimes chaotic!) years behind you, but look forward to what could be the best years of your life.

While retirement may seem a little way off, chances are you'll need to plan ahead to make the most of it. You may also need to think about your smaller goals along the way.

If you haven't had the time, or the inclination, to start thinking about your financial needs in retirement, it could be time you did.



This diagram illustrates the importance of various elements of financial advice. Moving from left to right, it also shows how much these elements can contribute to achieving your goals during your life.

The initial financial plan is only the starting point. Your adviser can provide you with financial advice, monitoring, reviewing and coaching throughout your entire life. He or she can revisit your goals and your financial situation, and if required, recommend changes to your financial strategies.

MEET *Tony and Joanne*

Tony is 54 and Joanne 49. They're married and their children have moved out of home. They both work full-time and earn salaries of $80,000 and $35,000 p.a. respectively.

Tony and Joanne have $100,000 and $30,000 in their respective super funds and have selected 'conservative growth' portfolios with approximately 50% invested in shares and property. They are receiving the minimum level of Superannuation Guarantee contributions from their employer (i.e. 9% of salary p.a.). Their super funds also provide life and TPD (total and permanent disability) insurance cover of three times their salary (including their accumulated super balances).

They have $10,000 in a savings account, $30,000 in a term deposit and $70,000 in a 'balanced' portfolio via an Investor Directed Portfolio Service ('IDPS')*. All three investments are in joint names and the after-tax income is being reinvested.

The couple owns a home valued at $500,000. However, they still owe $120,000 on their home loan and the minimum repayment is $1,393 per month for 10 years.

	TONY	JOANNE
Salary	$80,000 p.a.	$35,000 p.a.
Ongoing super contributions (at 9% p.a.)	$7,200 p.a.	$3,150 p.a.
Superannuation account balance	$100,000	$30,000
Savings account (joint names)	$10,000	
Term deposit (joint names)	$30,000	
IDPS investment (joint names)	$70,000	
Home value (joint names)	$500,000	
Home loan (joint names)	$120,000	
Home loan repayments	$1,393 (per month)	
Surplus cashflow (after living expenses)	$30,000 p.a.	
Inheritance (Tony)	$50,000	

After meeting their living expenses, they have a surplus cashflow of $30,000 p.a. (after-tax) to make additional home loan repayments and/or top-up their investments. Tony has also just received an inheritance of $50,000.

* An IDPS is an investment service that generally allows you to access a wide range of investment options and also provides consolidated reporting on those investment options.

WHERE DO THEY *want to be?*

The couple would like to retire in around 10 years, so they decide to seek financial advice to ensure they can live comfortably. With guidance from their financial adviser, they determine they'll need investments worth approximately $700,000 (in today's dollars) so they can achieve the retirement lifestyle they desire.

However, their adviser also helps them identify the other major goals they want to achieve between now and when they finish working. These include paying for their daughter's wedding at the end of the year, and buying a new car in three years.

WHAT	WHEN	HOW MUCH#
Pay for daughter's wedding	End of first year	$20,000
Replace car	Year 3	$20,000 (net of trade-in)
Fund retirement	Commencing in 10 years	$700,000

The table above summarises the lifestyle and financial goals Tony and Joanne identified with their adviser.

All figures are in today's dollars.

HOW WILL THEY *get there?*

In addition to helping define their goals, Tony and Joanne's adviser reviews their budget and assesses their current financial situation. He also recommends a range of clever strategies they hadn't even considered.

INITIAL ADVICE

HOME LOAN

They refinance their home loan into a facility that offers a 100% offset account.

SAVINGS ACCOUNT

They transfer the $10,000 from their savings account into the home loan offset account to save on interest and pay off their home loan faster. Because the offset account has ATM, internet and cheque book access, they are still able to access their emergency cash at all times.

TERM DEPOSIT AND INHERITANCE

They redeem the term deposit and use the $30,000 (as well as Tony's inheritance of $50,000), to reduce their home loan balance to $40,000. This strategy also delivers interest savings and enables them to eliminate their mortgage quicker. What's more, the money can still be accessed via a 'redraw' facility to pay for their daughter's wedding and their new car.

GEARING

Tony borrows $100,000 against the value of the family home, via a separate interest only investment loan. Because Tony pays tax at a higher marginal rate, he receives greater tax benefits from gearing than Joanne. The borrowed money is invested in a diversified share portfolio (via an IDPS), comprising a mix of Australian and global shares. Tony uses the tax benefits (as well as income from the investment) to help pay the investment loan interest.

INCOME PROTECTION INSURANCE

As Tony is the primary bread-winner (and because the investment loan is in his name), he takes out income protection insurance to replace up to 75% of his pre-tax income if he is unable to work due to illness or injury.

SUPERANNUATION

Their adviser explained that they're not just investing their superannuation for the ten years until they retire, but also for the 20 to 30 years they could spend in retirement. Recognising they still have a very long time horizon, Tony and Joanne decide to take a little more investment risk to help them reach their retirement goals. As a result, they both switch their super into 'growth' portfolios with approximately 85% invested in shares and property. Tony also arranges with his employer to salary sacrifice $1,000 per month (or $12,000 p.a.) of his pre-tax salary into his super fund. These contributions are in addition to the Superannuation Guarantee contributions Tony's employer has to make on his behalf.

BALANCED INVESTMENT THROUGH AN IDPS

To avoid triggering capital gains tax, they retain the $70,000 in the joint 'balanced' portfolio investment through an IDPS and continue to reinvest the after-tax income from this investment.

SURPLUS CASHFLOW

They use the balance of their surplus cashflow each month to pay off their home loan as soon as possible.

ONGOING ADVICE

Tony and Joanne also find that getting financial advice is not a one-off process. Their adviser reviews their goals and financial situation at least once a year and makes several ongoing recommendations.

HOME LOAN

They redraw money from their home loan to pay for their daughter's wedding (at the end of year one) and the new car (at the end of year three). Despite these withdrawals, they still pay off their home loan six years early (at the end of year four).

EMERGENCY CASH RESERVE

With their home loan paid off, they transfer their emergency cash reserve ($10,000) into a 100% offset account linked to their investment loan to reduce the interest bill.

REDUNDANCY PAYMENTS

At the beginning of year five, Joanne's role is made redundant after eight years service with her employer. She is entitled to an Eligible Termination Payment (ETP) of $8,076, consisting of accrued sick leave and a payment in lieu of notice. To save tax and make a larger after-tax investment, she decides to roll over the ETP into her super fund, rather than receive cash. Joanne is also entitled to a tax-free redundancy payment, as well as her accrued annual leave and long service leave. These payments must be taken as cash, so she 'parks' the after-tax amount ($24,194) in the investment loan offset account. This provides ready access to cash while she looks for new employment and helps them to save interest in the interim period.

SUPERANNUATION

Six months later, Joanne finds a new job paying a salary of $35,000 p.a. At this point, she withdraws the remaining cash redundancy payments from the investment loan offset account and uses the money to make an undeducted (after-tax) contribution into her super fund. In addition to boosting her super, this strategy entitles Joanne to a Government co-contribution. From year six, Joanne makes personal after-tax super contributions of $1,000 p.a., entitling her to Government co-contributions on an ongoing basis. Tony also increases his salary sacrifice contributions by $1,000 per month to create additional wealth for retirement in a tax-effective manner.

SURPLUS CASH FLOW

Going forward, all surplus cash flow is invested in the balanced investment held through the IDPS.

INVESTMENT LOAN

At the end of year 10, Tony repays the investment loan of $100,000. This will be achieved by selling sufficient units in the diversified share portfolio to cover the loan and capital gains tax on the amount withdrawn.

DIVERSIFIED SHARE PORTFOLIO

After repaying the investment loan, Tony retains the rest of the money in the diversified share portfolio. They also transfer the $10,000 emergency cash reserve from the investment loan offset account into a cash management trust in Joanne's name.

WHERE DO THEY *end up?*

When we wind the clock forward 10 years, Tony and Joanne have accumulated assets worth $1,054,825. This takes into account the money required for their daughter's wedding and the new car, as well as the income protection insurance cover.

However, you need to keep in mind that a dollar in the future won't buy what it does today. After taking into account an inflation rate of 3% p.a., the value of Tony and Joanne's portfolio in today's dollars is actually $784,889.

By following their adviser's recommendations, Tony and Joanne have comfortably achieved their goal of accumulating $700,000 (in today's dollars) when they retire.

WITH ADVICE∞	
Cash management trust (Joanne)	$10,000
Geared IDPS investment (Tony)	$74,934*
IDPS investment (joint)	$260,113
Superannuation (Tony)	$551,372
Superannuation (Joanne)	$158,406
Total	$1,054,825
In today's dollars that's	**$784,889**

∞ Assumptions: The home loan and investment loan interest rates are 7% p.a. Tony's geared share investment through the IDPS returns 8.5% p.a. (split 2% income and 6.5% growth). Tony selects a benefit period to age 65 and a waiting period of 12 months for his income protection insurance. Tony and Joanne's super funds each earn 8% p.a. (split 2.5% income and 5.5% growth). Tony's salary sacrifice super contributions are increased by 3% each year and he is not subject to the superannuation surcharge. The IDPS balanced portfolio (in joint names) returns 7.5% p.a. (split 3% income and 4.5% growth).

* This represents the balance of the geared IDPS investment, after repaying the investment loan of $100,000 and capital gains tax on the amount withdrawn.

TONY AND JOANNE'S *DIY approach*

Let's now wind the clock back and assume the couple decided they didn't need to see a financial adviser. As a result, they make the following choices:

SUPERANNUATION

They continue to invest their super in conservative growth portfolios.

SAVINGS ACCOUNT

They keep this account to provide for their emergency cash needs.

TERM DEPOSIT

They keep this account and use some of the money to pay for their daughter's wedding and new car.

BALANCED INVESTMENT THROUGH AN IDPS

They retain this investment and continue to reinvest the after-tax income.

INHERITANCE AND HOME LOAN

They use the $50,000 inheritance to reduce their home loan and continue to make the minimum home loan repayment of $1,393 per month.

SURPLUS CASHFLOW

They invest half their surplus cashflow in the term deposit and the rest in the balanced investment held through an IDPS.

REDUNDANCY PAYMENTS

At the beginning of year five, after Joanne is made redundant, they cash-out her ETP and pay lump sum tax. This money is then used (along with the cash redundancy payments) to eliminate their mortgage and the balance is parked in their savings account. Once Joanne finds work she will transfer the remaining cash to their term deposit.

SUPERANNUATION

With their home loan paid off, Tony arranges with his employer to salary sacrifice $250 per month ($3,000 p.a.) of his pre-tax salary into superannuation up until the point of retirement.

WHERE DO THEY END UP *(without advice)?*

After paying for their daughter's wedding and buying a new car, Tony and Joanne have accumulated investments worth $837,899. But remember we assumed an inflation rate of 3% p.a., meaning the value of their portfolio (in today's dollars) is only $623,476.

By taking a DIY approach, Tony and Joanne have fallen short of the $700,000 they needed to meet their lifestyle needs in retirement. Unless Tony and Joanne decide to work longer to accumulate more assets, they may need to revise their lifestyle expectations.

WITHOUT ADVICE∞	
Savings account (joint)	$10,676
Term deposit (joint)	$144,898
IDPS investment (joint)	$295,081
Superannuation (Tony)	$294,711
Superannuation (Joanne)	$92,533
Total	$837,899
But in today's dollars, that's only	**$623,476**

∞ Assumptions: Their super earns 7% p.a (split 4% income and 3% growth). The savings account earns 2% p.a. The term deposit earns 5% p.a. The home loan interest rate is 7% p.a. The IDPS balanced portfolio earns 7.5% p.a. (split 3% income and 4.5% growth). All distributions and interest are reinvested. Their salaries and living expenses increase at 3% p.a.

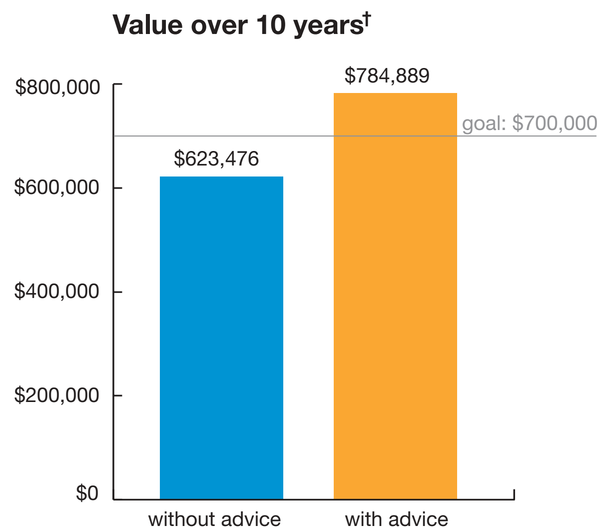
THE VALUE OF *advice*

The case study in this brochure, which is illustrative only, demonstrates that a properly structured financial plan (coupled with ongoing advice) can be the difference between reaching your financial goals and falling well short.

In this example, Tony and Joanne would have accumulated (in today's dollars) $623,476 without advice, compared to $784,889 by following the strategic recommendations of their adviser.

In all likelihood, your situation is very different from Tony and Joanne's, and the right advice for them is not necessarily the right advice for you.

If you really want to achieve your lifestyle and financial goals over the long-term, you should probably get started now.



† Assumptions: Salary, after-tax savings and pre-tax super contributions are indexed in line with inflation each year (at 3% p.a.). The overall level of franking on income is 15% for the superannuation conservative growth portfolio, 20% for the balanced portfolio held through an IDPS, 25% for the superannuation growth portfolio and 75% for the diversified share fund (Australian income only) held through an IDPS. Investment earnings are taxed each year (at marginal tax rates, except for superannuation, which is taxed at 15%). Except for repaying the investment loan, Tony and Joanne don't cash out their investments, so capital gains tax and lump sum taxes do not apply until the investments are actually realised.

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