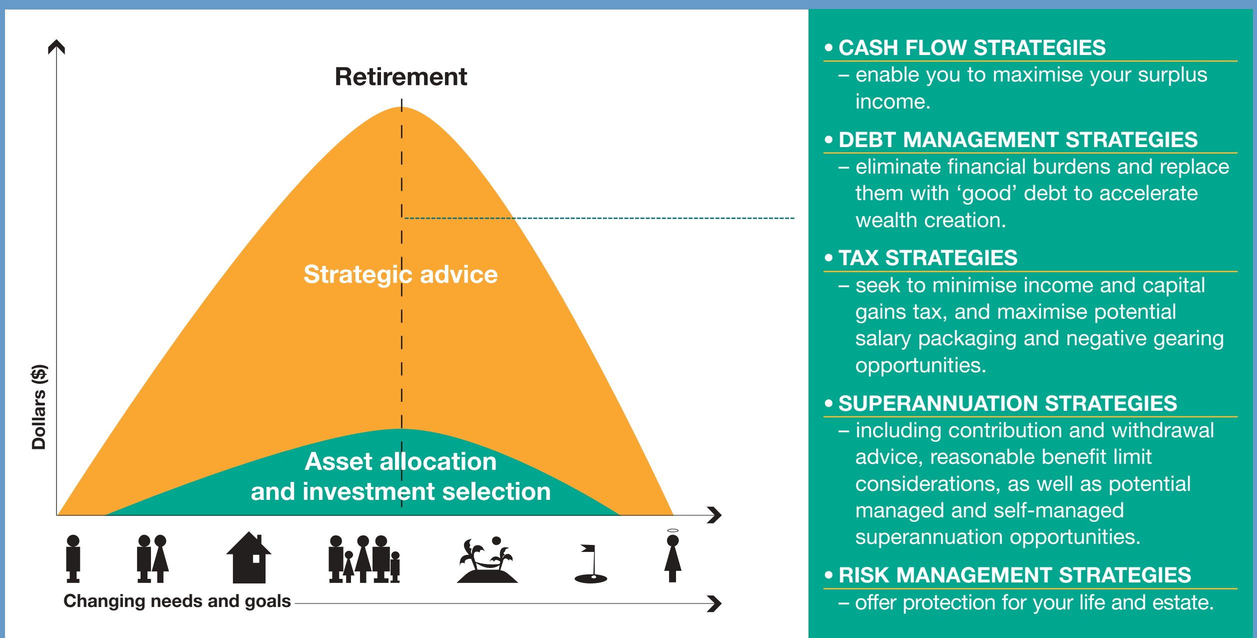
THE VALUE OF ADVICE FOR *seniors*

Retirement could be just around the corner. The years of alarm clocks and deadlines are almost behind you, and it will soon be time to enjoy yourself.

Naturally, you want to make the most of what you've worked so hard to achieve. And you needn't go it alone. Good financial advice can help make the difference between a good retirement and a great retirement.



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 *Ken and Diane*

Ken (aged 65) is about to retire, while Diane (aged 63) has already retired. Ken has a superannuation benefit worth $280,000.

They also have $10,000 in a savings account, $30,000 in a 'balanced' portfolio via an Investor Directed Portfolio Service ('IDPS')*, and $60,000 in a term deposit. All three of these investments are held in joint names.

Ken and Diane own a home worth approximately $400,000 and have lifestyle assets (including the family car and home contents) valued at around $35,000.

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

Savings account (joint names)	$10,000
IDPS investment (joint names)	$30,000
Term deposit (joint names)	$60,000
Superannuation (Ken)	$280,000
Total	$380,000

WHERE DO THEY *want to be?*

Ken and Diane are both in good health and realise their investments will need to last a long time. So they decide to see a financial adviser to find out what they should do with their money.

The first thing their adviser does is help them identify their lifestyle and financial goals. After reviewing their needs, their adviser estimates they'll need an after-tax income of $32,000 each year. To ensure their purchasing power is maintained, this income will be indexed at an assumed inflation rate of 3% p.a.

Along the way, they have some major expenses that need to be met. These include an overseas trip (in three months) and a new car in five years. They would also like their children to inherit the family home, plus investments worth approximately $100,000 (in today's dollars).

WHAT	WHEN	HOW MUCH#
Living expenses	Starting now	$32,000 p.a.
Overseas trip	3 months	$10,000
Car	5 years	$20,000 (net of trade-in)
Provide inheritance	Unknown	Family home, plus investments worth $100,000

The table above summarises the goals the couple identified with their adviser.

All figures are in today's dollars.

HOW WILL THEY *get there?*

In addition to helping them define their goals, Ken and Diane's adviser assesses their complete financial situation and recommends a range of clever strategies they hadn't even considered.

SAVINGS ACCOUNT

They transfer the $10,000 into a Cash Management Trust (CMT) in Diane's name. With the CMT, they are still able to access the cash in the event of an emergency. However, they earn a higher interest rate than the savings account and tax is payable at Diane's lower marginal rate.

INVESTMENT THROUGH AN IDPS

While they leave the $30,000 invested through the IDPS, they reinvest income distributions so they can purchase more units and benefit from compound returns.

TERM DEPOSIT

They keep $10,000 in the term deposit to pay for the holiday in three months and withdraw the remaining $50,000. Because Diane is under age 65, Ken is then able to use the $50,000 to make a spouse contribution into a superannuation fund in Diane's name. This enables Ken and Diane to split income in a tax-effective manner.

KEN'S SUPER

Ken can access his super when he retires. Furthermore, because his super consists entirely of Post June 1983 benefits, he can withdraw up to $123,808 (in 2004/05) without paying any tax. To take further advantage of income splitting, Ken cashes out $120,000 and makes another spouse super contribution on Diane's behalf.

ALLOCATED PENSION (IN DIANE'S NAME)†

Diane uses her super benefit of $170,000 (i.e. $50,000 from the term deposit and $120,000 from Ken's super) to purchase an allocated pension. The allocated pension is invested in a balanced portfolio and she draws the Government prescribed minimum income each year to preserve their capital. As the purchase price consists entirely of undeducted contributions, Diane's capital is returned on a tax-exempt basis over the life of the income stream. Any taxable income payments are also eligible for a 15% pension offset. Finally, lump sum withdrawals (commutations) can be made from an allocated pension at any time. Therefore, Diane redeems enough funds from her allocated pension to buy their new car in five years time.

TERM ALLOCATED PENSION (IN KEN'S NAME)†

Ken uses the rest of his super ($160,000) to purchase a term allocated pension (TAP). The TAP is invested in a balanced portfolio and Ken selects a term of 22 years. While Ken is not able to make lump sum withdrawals from this investment, 50% of the purchase price (and ongoing account balance) is exempt from the social security Assets Test. As a result, investing in a TAP helps Ken and Diane qualify for more Age Pension payments. Also, the taxable income payments attract a 15% pension offset.

SURPLUS INCOME

Any surplus income each year is invested through the IDPS.

† Diane's allocated pension and Ken's TAP are also treated favourably under the social security Income Test.

WHERE DO THEY *end up?*

By following their adviser's recommendations, Ken and Diane exceeded their after-tax income goal of $32,000 in the first year (see table below). You'll also note they received significant Age Pension benefits and didn't have to pay any tax.

INCOME IN YEAR ONE∆	KEN	DIANE	COMBINED
Cash management trust	$0	$450	$450
Allocated pension	$0	$10,240	$10,240
Term allocated pension	$10,550	$0	$10,550
Age Pension*	$6,223	$6,223	$12,446
Total income∞	$16,773	$16,913	$33,686
Tax payable/(refund)	($39#)	($39#)	($78#)
Net income∞	$16,812	$16,952	$33,764

* Age Pension figures are current as at 20 March 2005.

These figures represent a refund of excess franking credits on the income distributions from the investment through the IDPS (franking level 20%).

∞ All figures are in today's dollars.

When we wind the clock forward, they continue to meet their income needs (i.e. $32,000 p.a. indexed at 3%). After 20 years, they also have investments worth a total of $459,678∆, after paying for their overseas holiday (in year one) and new car (in year five).

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 Ken and Diane's portfolio (in today's dollars) is $254,512.

Given their life expectancy is another 6.11 years for Ken and 8.27 years for Diane, they still have enough money to enjoy a comfortable retirement and provide an inheritance of $100,000 (in today's dollars).

VALUE OF INVESTMENTS AFTER 20 YEARS∆	
Cash management trust (Diane)	$10,000
IDPS investment (joint)	$279,102
Allocated pension (Diane)	$122,678
Term allocated pension (Ken)	$47,898
Total	$459,678
Total in today's dollars	**$254,512**

∆ Assumptions: The CMT earns 4.5% p.a. No withdrawals are made from the investment through the IDPS and all returns are reinvested. The IDPS investment earns 7.5% p.a (split 3% income and 4.5% growth) and the franking level on income was 20%. Diane's allocated pension and Ken's term allocated pension (both of which are invested in balanced portfolios) earn a total return of 7.5% p.a.

TONY AND JOANNE'S *DIY approach*

Let's now wind back the clock and assume Ken and Diane didn't seek financial advice. As a result, they make the following choices:

SAVINGS ACCOUNT

They leave the $10,000 in this account to provide for their emergency cash needs.

INVESTMENT THROUGH AN IDPS

They retain this investment (currently worth $30,000) and receive the income each year rather than reinvest it.

KEN'S SUPER

Ken cashes out his $280,000 super benefit, so they can 'get their hands on the money'. While he receives the first $123,808 tax-free (in 2004/05), his remaining benefit is taxed at 16.5%. As a result, he has to pay $25,772 in lump sum tax, reducing his net pay out to $254,228.

TERM DEPOSIT

They keep the $60,000 currently invested in the term deposit and make an additional investment of $254,228 using Ken's after-tax super benefit. The initial balance is therefore $314,228. They also withdraw from this account to pay for their holiday (in three months) and new car (in five years).

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

By taking a do-it-yourself approach, Ken and Diane did not receive enough Age Pension benefits and investment income to meet their after-tax goal of $32,000 in the first year (see table opposite). As a result, they needed to withdraw over $7,000 from their term deposit to make up the shortfall.

INCOME IN YEAR ONE∆	KEN	DIANE	COMBINED
Savings account	$100	$100	$200
IDPS investment	$450	$450	$900
Term deposit – interest	$7,606	$7,606	$15,212
Age Pension*	$4,108	$4,108	$8,216
Total income∞	$12,264	$12,264	$24,528
Tax payable/(refund)	($39#)	($39#)	($78#)
Net income∞	**$12,303**	**$12,303**	**$24,606**
Additional money withdrawn from term deposit			$7,394
Money required to meet lifestyle goals			**$32,000**

* Age Pension figures are current as at 20 March 2005.

This figure represents a refund of excess franking credits on the income distributions from the IDPS investment (franking level 20%).

∞ All figures are in today's dollars.

Over the years, the additional withdrawals required to meet their living expenses put a big dent in the value of their term deposit. Consequently, their portfolio is only worth $202,904 in 20 years (after also taking into account the money required for the holiday and new car).

But remember we assumed an inflation rate of 3% p.a., so this means the value of their investments (in today's dollars) is only $112,343. In other words, Ken and Diane won't have enough money to maintain their standard of living, as well as pass on an inheritance of $100,000 (in today's dollars).

VALUE OF INVESTMENTS AFTER 20 YEARS∆	
Savings account (joint)	$10,000
IDPS investment (joint)	$72,351
Term deposit (joint)	$120,553
Total	$202,904
Total in today's dollars	**$112,343**

∆ Assumptions: The savings account earns 2% p.a. The term deposit earns 5% p.a. The balanced investment through the IDPS earns 7.5% p.a (split 3% income and 4.5% growth) and the franking level on income was 20%. No withdrawals from the investment through the IDPS have been made.

THE VALUE OF *advice*

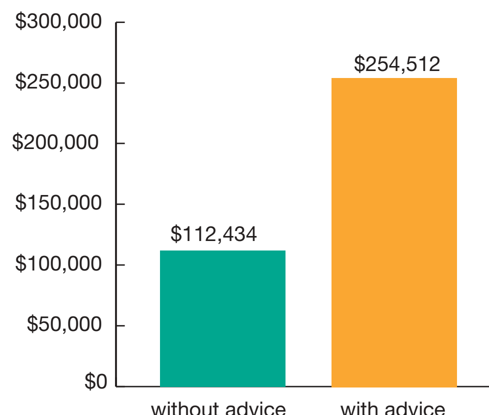
The case study in this brochure, which is illustrative only, demonstrates that a properly structured financial plan can be the difference between reaching your financial goals and falling well short.

In this example, Ken and Diane would have remaining assets worth $112,343 without advice, compared to $254,512 by following their adviser's strategic recommendations.

In all likelihood, your situation is very different from Ken and Diane'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, you should get started now. And the best place to start is to talk to a financial adviser.

Value over 20 years∞



∞ Assumptions: The annual income required by Ken and Diane, the Age Pension payments and various social security thresholds are indexed in line with inflation each year (3% p.a.). The overall franking on income is 20% for the IDPS. Income from the investments are taxed each year at marginal tax rates. Where applicable allowances have been made for any deductible amount or tax offsets.

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