Centuria

When super alone is not enough

Superannuation can be a tax effective way to invest for retirement. With changes to superannuation coming into effect on 1 July 2017, there may be some limits and constraints with superannuation and some investors and financial advisers may be looking for an alternative tax effective structure like an investment bond.

Case study: What's next when superannuation contributions have been maximised

Anthony is 45 years old and has invested wisely in the property market. However, he now believes that property returns have plateaued and has therefore sold his inner-city investment property and realised a healthy capital gain.

He has paid off his mortgage and maximised his superannuation contributions, both concessional and non-concessional contributions.

Anthony wants to know how to best invest his surplus proceeds of $200,000 tax effectively to generate the potential for solid returns. He earns a good income and does not need access to his funds and therefore can adopt a long-term investment time horizon of 10 years plus.

He considers investing in Australian shares either via a managed fund, directly in the sharemarket or via his family trust, and taking advantage of franking credits that can reduce the tax paid which is important to him given that he is on the highest marginal tax rate.

His adviser suggests that he can still access the benefits of franking credits from Australian shares and access a tax effective structure, by investing the funds in an investment bond (Australian shares option), which pays a maximum tax of 30%. However, the franking credits from the shares can reduce the effective tax rate paid by the investment bond.

In addition, Anthony can afford to invest additional amounts of $10,000 into the investment bond for the first three years as he is unable to direct any surplus funds into superannuation without exceeding his contribution caps. In three years' time, he plans on reducing this annual contribution amount he invests to $5,000 per year.

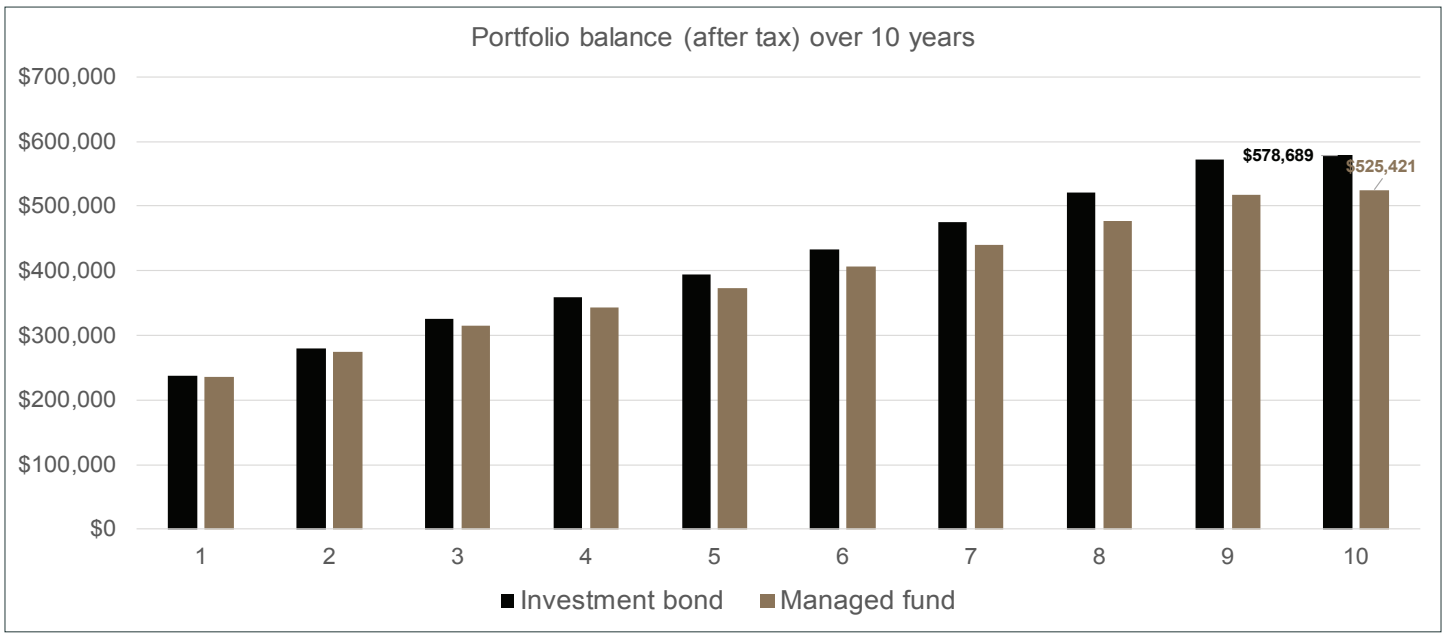
His adviser confirms that he can redeem his investment bond and pay no additional tax after 10 years from the initial investment provided the additional contributions do not exceed 125% of the previous year's contributions.

When Anthony reaches age 55, the investment bond has accumulated to approximately $551,6461 (tax paid). This is estimated to be $35,763 higher than the alternative of investing at his personal marginal tax rate.

	Strategy advantages:
✓	• The investment bond benefits from the franking credits from shares and the maximum tax rate of 30%. In this scenario, it is estimated that it results in a higher balance by $35,763 compared to investing in a managed fund, directly in the sharemarket or via his family trust (whereby he will be taxed at his marginal tax rate). • Tax is paid at the 30% corporate tax rate and the money can be withdrawn after 10 years with no further tax paid. However, earlier withdrawals may see all or some of the growth withdrawn taxed at marginal tax rates. • The investment bond provides an easy solution i.e. no need to declare the earnings in annual tax returns. • The 30% tax rate is a lower tax rate than his individual marginal tax rate. However, after allowing for dividend imputation credits and other tax deductions, the effective tax rate for the investment bond may be lower2. • The underlying investment options within the investment bond range from conservative to high growth to match the client's risk profile.

The net sum available in the investment bond in 10 years' time by comparison to the same return achieved within a managed fund tax structure that is taxed at Anthony's marginal tax rate is shown in the graph on the following page. It is important to note that this is illustrative example based on specific assumptions noted. Advisers are encouraged to consider the assumptions and run their own calculations.

Portfolio balance (after tax) over 10 years ($53.4K higher than investing at his personal marginal tax rate)



Provided for illustrative example only based on the basic income and growth assumptions described above. This illustrative example does not purport to represent the actual return possible in any of Centuria Investment Bonds. An investment is subject to risk, the degree of which depends on the assets in which the bond invests. Assumptions: 1. Total returns of 8.5% (4.5% income (80% franked), 4% capital growth) per annum, 100% annual turnover of the portfolio, 50% CGT discount applies for managed fund.

- Doesn't take into account the fees of any structure. Fees may impact materially on the final outcome.
- The composition of income vs growth in a return will also have an impact on the outcome. Generally, the higher the growth component the greater the benefit of CGT tax discounting for an investment through the managed fund structure. This will change the outcome.
- Advisers are encouraged to undertake their own research based on the risk tolerances and investments to be selected by their clients.

If Anthony had chosen to invest the $200,000 into a discretionary family trust rather than investing the funds in a managed fund in his own name, the results would essentially be the same as investing in his own name. This is because the discretionary trust does not pay tax as the earnings are passed onto the beneficiaries and they pay tax at their marginal tax rate.

A discretionary family trust can provide the ability to choose who to make the distributions to if there are multiple beneficiaries on different marginal tax rates. However, an investment bond can be a more attractive option considering:

- Anthony is the only beneficiary; and
- The complexity and cost of establishing and running a trust e.g. costs of producing annual financial and tax accounts.

Benefits of an investment bond:

1. **No limit on the investment amount:** There is no limit on the amount that can be invested in an investment bond in the first year and you can invest up to 125% of the previous years contributions each year thereafter.
2. **Flexibility:** Investment bonds provide the flexibility to access money at any time which can act as a hedge against the restricted access for superannuation.
3. **Tax simplicity:** Investment bonds provide simplicity as earnings are automatically reinvested in the bond and tax is paid within the bond.
4. **Estate planning:** the death benefit form an investment bond is paid tax free to the beneficiary.
5. **Bankruptcy protection:** Investment bonds may offer protection from creditors in the case of bankruptcy.

Start investing today.

Simple | Flexible | Versatile

For more information contact Centuria on 1300 50 50 50 or visit www.centuria.com.au/investment-bonds to download the PDS.

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