

# Financial Planning and Investment

Travis Morien, Updated November 2004

Investment risk and the asset classes .....	4
Investment risk .....	4
Types of investment risk .....	4
The asset classes .....	5
Expectations of future returns from the asset classes .....	11
Portfolio construction .....	12
Asset allocation - basic principles of portfolio construction .....	12
Risk and return of model portfolios .....	14
Why is asset allocation so important? .....	20
Strategic asset allocation vs. tactical asset allocation .....	22
Choosing investments .....	23
Index funds .....	23
Active funds .....	25
Criteria for choosing active managed funds .....	25
Retail vs. Wholesale Funds .....	29
Direct investments .....	29
Wrap accounts and Master Trusts .....	30
How to value companies on the stock market .....	32
The difference between investment and speculation .....	32
Defensive vs. enterprising investors .....	33
Winners and losers .....	34
The theory of intrinsic value .....	34
The time value of money .....	35
The investor and market fluctuations .....	36
Identifying a superior business opportunity .....	36
Financial criteria identifying a superior business .....	38
Non-financial criteria .....	39
Simple valuation models .....	40
Absolute models .....	40
Relative models .....	43
How reliable are projections of growth in earnings and sales? .....	43
Implications these studies to stock picking .....	44
Selecting an appropriate stock selection policy .....	45
Reading company accounts .....	46
Profits vs. cash flows .....	48
Portfolio maintenance and ongoing management .....	50
Rebalancing a portfolio - reducing risk and increasing return .....	50
Long term holding periods .....	51
Dollar cost averaging .....	52
Value averaging .....	53
Approaching retirement .....	54
Tax planning .....	55
Overview of tax planning .....	55
The boundaries of tax planning .....	55
Tax planning strategies .....	56
Paying off non deductible debt .....	56
Income splitting .....	56
Favour capital growth investments .....	56
Hold long term .....	57
Time your capital gains .....	58
Offset capital gains with losses .....	58

Salary sacrifice .....	59
Gearing .....	59
Tax deductible primary production schemes.....	61
Foreign income.....	63
Minors income .....	64
Insurance bonds.....	65
Tax structures and entities .....	66
Individual ownership.....	66
Partnership.....	66
Trusts .....	67
Discretionary trust.....	68
Fixed trust.....	68
Franking credit trading rules.....	69
Family trust election.....	70
Companies .....	71
Superannuation fund .....	73
Comparison table .....	75
Combining structures.....	78
Corporate trustees .....	78
Sections of the Act to be wary of.....	79
Loans between entities.....	79
Personal services income.....	79
Superannuation.....	80
What is superannuation?.....	80
Contribution taxes and contributions surcharge.....	80
Eligibility to contribute to superannuation.....	81
Employer contributions and choice of fund.....	81
Tax deductibility of superannuation contributions .....	82
Splitting of superannuation between spouses.....	83
Spouse contributions tax offset and co-contributions.....	83
Conditions of release from superannuation .....	84
Reasonable benefits limits (RBL).....	86
Components of superannuation.....	88
Retail superannuation funds .....	90
Superannuation Master Trusts .....	90
Self Managed Super Funds (SMSFs).....	90
Bringing foreign super funds into Australia .....	92
Gearing.....	93
What is gearing? .....	93
What are the advantages of gearing?.....	93
What are the risks of gearing?.....	94
Forms of credit .....	95
Minimising the risks of gearing .....	96
Asset protection planning.....	98
Asset protection introduction .....	98
The golden rule of asset protection strategies .....	99
Types of risk and major asset protection issues .....	99
The steps of risk management .....	100
Alternatives for handling risks.....	100
Vulnerable professionals and businessmen.....	101
Bankruptcy .....	101
Vulnerable dealings.....	103
What happens after discharge?.....	104
Ownership of assets.....	104
Risk management suggestions for company directors.....	106

Proposed changes to the Bankruptcy Act .....	107
Life and disability insurance .....	108
Types of insurance available .....	108
Group rate cover .....	109
Stepped or level premiums .....	111
Retirement Planning .....	113
Asset allocation and income planning.....	113
Retirement income streams .....	116
How superannuation income streams are taxed .....	116
Allocated pensions and annuities .....	116
RBL compliant pensions and annuities.....	118
Comparison of income stream products .....	120
Income stream strategies .....	121
Complying pensions and social security .....	122
Complying pensions and the pension RBL .....	123
Estate Planning.....	126
What to consider with estate planning .....	126
Estate planning glossary: .....	126
Wills .....	128
Testamentary Trusts.....	128
Powers of Attorney .....	129
Assets not included in the estate .....	130
Options for dealing with superannuation.....	131
Lump sum payments.....	131
Income streams .....	132
Binding death nominations.....	133
Ideal structure of estate .....	134
What is the general procedure?.....	134
When is a Will a "valid" Will? .....	135
Important considerations in choosing Executors.....	135
Dealing with debts .....	136
How can distributions under a Will be challenged? .....	136
What if there is no Will? .....	136
Business succession planning .....	137
What is business succession planning?.....	137
Why set up a business succession plan? .....	137
Business succession agreements.....	138
Funding a business succession agreement.....	138
Business expenses insurance .....	139
Forms of business succession agreement.....	139
Ways to transfer ownership of the business .....	139
Valuation of the business .....	140
Ownership of insurance policies .....	141
Business succession agreements and taxation .....	141
Capital Gains Tax rollover relief.....	143
Business succession agreements and your Will .....	143
Alternative funding arrangements.....	144
Key man insurance.....	144
Appendix one A: Australian life tables 1995-97 .....	145
Appendix one B: Australian life tables 2000-02 .....	146
Appendix two: Allocated Pensions Pension Valuation Factors .....	147
Appendix three: Term Allocated Pension Payment Factors.....	148
Appendix four: Age pension and Newstart, rates and tests .....	149
Appendix five: Australian tax rates and offsets 2004/05 tax year.....	155
Appendix six: FINANCIAL SERVICES GUIDE .....	159