

Perpetual's monthly technical guide

In this special edition of Tech Time, we explain how WealthFocus Investment Advantage, our innovative investment offering can give your clients better portfolio construction and taxation outcomes.

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A platform with a unique tax structure

WealthFocus Investment Advantage can give your clients something they won't find anywhere else – platform benefits with the ability to move between investment options without incurring capital gains tax (CGT).

We understand that from time to time your clients will need to switch investment options or redeem their investments.

WealthFocus Investment Advantage is no ordinary platform. It offers a range of **over 80 investment options within a single fund**, which you can combine to create a portfolio unique to your client. This allows them to move their money across asset classes or investment managers while reducing the CGT consequences.

How it works

Your client acquires one unit in the fund with their initial investment. Your client's unit value is calculated based on the proportion of each investment option held in their portfolio and the value of the investment options in their portfolio.

Example portfolio structure for a \$10,000 investment

- Investment Option 1 - \$5,000
 - Investment Option 2 - \$3,000
 - Investment Option 3 - \$2,000
- = 1 unit**

What are the tax benefits?

- **CGT-free switching.** You can move your clients across asset classes and managers without triggering CGT.
- **CGT-free partial withdrawals until the cost base is reduced to zero.** Partial withdrawals will not incur CGT unless the withdrawal amount exceeds the cost base of the unit.
- **If the initial investment is held for more than 12 months, the CGT discount applies to all investments.** Additional investments in WealthFocus Investment Advantage will not alter the acquisition date.

All of these unique tax benefits are backed by an ATO product ruling (PR 2008/62).

The following case studies illustrate the benefits in practice.

Case study 1 – tax-effectively manage auto rebalancing


Bob and Sally wish to invest \$100,000 across several investment funds. They want to use an auto rebalancing option to ensure their portfolio maintains a consistent exposure across the asset classes.

However, they are concerned that the frequent switching resulting from the auto rebalancing will reduce the effectiveness of the strategy, as it will regularly trigger CGT. In most cases, the resulting gains will be short-term gains, and therefore not eligible for the 50% CGT discount. Further, the tax is payable annually with the lodgement of their tax returns, which would decrease the amount available to invest.

Bob and Sally's financial adviser recommends they invest in WealthFocus Investment Advantage to minimise these problems.

Benefits

- Capital gains won't be triggered every time the portfolio is rebalanced. Instead, any capital gains incurred will be deferred until the investment in the platform is fully redeemed.
- Any capital gain triggered will be reduced by half, provided at least 12 months has passed since the initial investment. This means that Bob and Sally's financial adviser can focus on optimising the investment strategy without being influenced by tax issues that may otherwise apply over the life of the investment.

 **Tech tip:** Even when Bob and Sally fully redeem the investment, effective tax planning can minimise the tax payable. For example, by redeeming the asset over a number of years they could prevent their income being pushed into a higher tax bracket. Alternatively, they could defer the realisation until they retire.

Case study 2 – tax-effectively re-weight towards cash

Janet is worried about market performance over the next 12 to 24 months. She is also concerned about her job security over this period. She may need to redeem some of her managed investments at short notice if she loses her job, so would like to switch into a cash option.


Janet has been invested in managed funds for several years, and is aware that if she implements this strategy she will trigger significant capital gains. However she is prepared to wear this cost to ensure her peace of mind. She will again invest in higher-growth managed funds when her outlook on investment performance is more positive.

Janet also plans to take a year off work in about five years' time to travel the world, using the balance of her investments at that time to fund her income requirements.

Janet speaks to her financial adviser, who recommends that she redeems her managed funds and invests the proceeds in the cash option within WealthFocus Investment Advantage.

Benefits

- When Janet is ready, she can easily switch from cash into higher-growth investment options offered by the platform.
- If Janet withdraws funds to meet her income requirements, she will not trigger a capital gain until she withdraws more than her initial investment amount including additional investments.
- If Janet chooses to re-weight the portfolio in the future, she will not trigger capital gains.
- Although CGT may still be payable when she eventually redeems her investments in full, she will qualify for the 50% discount provided at least 12 months has passed from when the first dollar was invested.

 **Tech tip:** The ideal time for Janet to fully redeem her investments in WealthFocus Investment Advantage would be when she takes a year off from work, as at this time she will have minimal other income and a lower marginal tax rate.

Case study 3 – tax-effectively manage a regular savings plan

Nicole and Peter have inherited a large sum of money, which they wish to invest in a diversified portfolio, in regular amounts staged over the next two years. With the advice of their financial adviser they invest in the WealthFocus Investment Advantage platform.

Due to unforeseen circumstances, Nicole and Peter need to cash out their investment soon after their last regular contribution. Their portfolio has performed strongly, which means they are now facing a significant capital gain.

Benefit

- Since Nicole and Peter were invested in WealthFocus Investment Advantage and the initial investment was made more than 12 months ago, the entire capital gain is reduced by half. Had they been invested in a regular platform, only the first 12 months' worth of contributions would qualify as long gains and be eligible for the 50% discount. Any gains on contributions made within the last 12 months would be 100% assessable as they do not satisfy the minimum 12 month holding rule.

Case study 4 – tax-effectively manage regular withdrawals

Jim and Judy have recently had twins. Their financial adviser recommends they set up an investment plan using WealthFocus Investment Advantage to provide for the twins' secondary school education in 12 years' time. Jim and Judy invest \$60,000 across three different funds chosen by their adviser from the investment menu.

The adviser actively manages Jim and Judy's portfolio over the next 18 years, switching funds a number of times as the economy changes and the chosen funds change their characteristics.

Benefit

- WealthFocus Investment Advantage can offer Jim and Judy a highly diversified portfolio, with access to more than 80 high quality managed funds across a range of investment managers and asset classes.
- On any other platform, Jim and Judy would have to pay CGT when the switches are made, but with WealthFocus Investment Advantage switches do not trigger CGT. Jim and Judy's portfolio can therefore be updated without being diminished by a tax payment.

In the 12th year, Jim and Judy begin drawing down \$10,000 pa for the six years that the twins are in secondary school. They keep the remaining balance invested in WealthFocus Investment Advantage as a saving towards their retirement.

Benefit

- Jim and Judy can make partial withdrawals up to the amount originally invested (including additional investments) without triggering CGT. Using any other platform, Jim and Judy would pay CGT when the withdrawals are made.

Jim and Judy keep their remaining investment in WealthFocus Investment Advantage as a saving for retirement. However, before they reach retirement they have a family medical crisis and withdraw a large proportion of the investment to meet the costs. Because they withdraw more than they have invested, they now must start paying the capital gains tax liability that has accrued. They have reinvested their last two sets of distributions. These amounts have been in the funds for less than 12 months.

Benefit

- Jim and Judy get a CGT discount on the gain that accrued on the reinvested distributions. With any other platform, the 12 months would be counted from the day that the distributions were reinvested, but with WealthFocus Investment Advantage the 12 months is counted from the day the very first investment is made.

Jim and Judy emerge from the crisis and start rebuilding their investment in WealthFocus Investment Advantage, although the portfolio is now completely different to how it started out. Many years later they start withdrawing amounts to meet their living expenses in retirement.

Benefit

- Jim and Judy are paying CGT on the gain that has accrued over the decades, but are now on a much lower marginal tax rate than they were at the time they were switching funds and making the earlier withdrawals. They are therefore paying less tax on these gains than they would have on any other platform, as well as paying it at a much later time.

Case study 5 – tax-effectively manage an SMSF portfolio

The members of The Simpson Self Managed Super Fund wish to invest a portion of the Fund's assets across a range of managed funds. To ensure the Fund's investment allocation remains consistent with its investment strategy, they elect to use auto rebalancing. They will also withdraw some of their funds once their investments reach a certain level.

The Fund's financial adviser recommends that it invests in WealthFocus Investment Advantage.

After several years, two members of the Fund retire and commence pensions.

Benefits

- With WealthFocus Investment Advantage, the Fund will not incur any tax when the portfolio is adjusted as a result of auto rebalancing.
- On any other platform, the Fund would be required to pay tax of up to 15% on the unrealised gains.
- The Fund will not incur any CGT when withdrawals are made from the platform unless the amount of the withdrawals exceeds the cost base.
- Even though a significant amount of gains have been built up over the years, by deferring the realisation of these gains until the members are in pension phase, there won't be any CGT payable.
- The potential benefit could run into tens of thousands of dollars when one considers the gain that could accrue over an eight year period.

This analysis has been prepared by Perpetual Investment Management Limited (PIML) ABN 18 000 866 535, AFSL 234426 Perpetual Superannuation Limited (PSL) ABN 84 008 416 831 AFSL 225246 RSE L0003315 for the use of financial advisers only, it is general information and is not intended to provide you with financial advice. The technical interpretations expressed in the article are the opinions of the author at the time of writing and do not constitute a recommendation to act. Any information referenced in the article is believed to be accurate at the time of compilation and is provided by Perpetual in good faith. To the extent permitted by law, no liability is accepted for any loss or damage as a result of any reliance on this information.

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Further information

Adviser Services 1800 062 725

Investor Services 1800 022 033

Email investments@perpetual.com.au

www.perpetual.com.au