Financial Freedom

QUARTER 2 2011 NEWSLETTER

OUR SERVICES

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INSIDE THIS ISSUE:

A Widely Diversified Share Portfolio Is A Safe Haven In Inflationary Times

In his historic first media conference in late April, US Federal Reserve Chairman Ben Bernanke made repeated references to inflation. He confirmed that central bankers around the world are taking the challenge seriously, and will do what it takes to manage inflation - banker speak for putting up interest rates.

In New Zealand, inflation for the year to March 2011 has risen to 4.5%, albeit helped by the recent increase in GST. We have all seen the increases in food and petrol prices as well. Internationally, Australia's Reserve Bank, has already started hiking rates to around their long term average of 4.75% from a low of 3.0% in 2009 to address inflationary concerns. China has long been worried about the inflationary effects of its sustained economic transformation, having raised rates four times recently. With so many of New Zealand's regional trading partners enjoying the kinds of robust economic growth most developed countries can only dream of, whatever the fragility of our own economy following the earthquake, inflationary momentum will be hard to resist.

What does this have to do with investors and savers? Since the stock market crash of 2007 - 2009, many people have sworn off shares, opting for the apparently safer harbours of fixed interest, bonds and bank deposit accounts. This is supported by ASB's Investor Confidence survey, showing term deposits are seen as the best returning investment. While this reaction is entirely understandable, and it is true that bank fixed interest and savings accounts are as reliable as you'll get, the truth is that as a place to keep all your core wealth over the long term they can only guarantee one thing - that the true value of your investment will enjoy minimal, if any, growth.

The safe harbour of cash and bonds may well suit those people already some way into retirement, and such investments should be considered as part of an investors' overall portfolio. You will certainly be protected from the kind of volatility you experience as share portfolios rise and fall. But the rest of us need to invest at least some of our core wealth in well diversified asset classes that deliver stronger performance. That 5% or 6% return from a bank or government bond can translate into a mere 1% or 2% return (or less!) after we account for inflation and tax. And there are those who have good reasons to suggest that inflation is actually eating away the value of our dollar at a higher rate than the current inflation rate suggests.

One of the long understood principles of investing is the direct relationship between risk and return. This is not an encouragement to be reckless and take on unrewarded risk – as so many failed finance companies and speculative investments have persuaded unfortunate investors to do in the past. Rather it suggests that, as well as the safe haven of cash and bonds, we should allocate some of our long term investments to globally diversified portfolios of shares and property, if we want to participate in the long term growth that these asset classes have traditionally enjoyed. Higher returns require higher risk.

Looking at the returns of many diversified funds over the past 12 months, we're seeing growth of 8%. This is despite all the peaks and troughs of the past year with its worries about European sovereign debt, North African instability and most recently the impact of Christchurch and Japan's earthquakes. If that level of growth can be achieved amid such volatility, it is easy to envisage even more robust performance as the global economic recovery strengthens.

It may seem counter-intuitive to think of shares as providing the real safe haven. But a widely diversified portfolio certainly offers much greater protection than fixed interest rates, as the global recovery - and rising inflation - take hold.

Take Charge of Your Finances

With prices increasing every day it is important to make your very own strategic plan on maximising your finances and making sure every cent earned is well spent.

Your source of income, lifestyle, spending habits, current job and house location, cost of living, expenses and loans determine your level of budgeting needs. Taking charge of your finances is one sure way of feeling a sense of achievement and control.

- Treat maths as your friend, compare prices and quality for everything you buy.
- Gambling– this strips you of your money, it tops the chart in making life chaotic
- Know the difference between wants and needs
- Do not spend more than you earn
- Keep a list, have a weekly/monthly budget
- Emergency fund, for just that!
- Savings & investment, pay yourself first
- Seek out professional advice

Medical Corner

"There is no such thing as a problem, only an opportunity to do things differently"

Unknown

This month we look at men's health, and what check-ups men of all ages should be having to help identify small problems before they turn into serious issues. It could literally save your life!

By Dr Graeme Washer MB, CHB, FRACS

Trustee, Men's Health Trust
General and Colorectal Surgeon at Auckland's Ascot and Integrated Hospital
Part-time General Practitioner

We get a Warrant of Fitness (WOF) on our cars, so why not on our health?

A possible consequence of not having a current WOF on your car is receiving a fine. For ourselves, it could be health problems later on in life, and the penalty may be a lot more than you expected or want to pay!

Men of all ages should ensure they get a WOF health check up each year. This 'Well Man' consultation is important to identify and work with your doctor to alter your specific health risks, rather than waiting for symptoms or illness to develop.

So what needs to be done at the check up?

The doctor will take information such as your:

- Age
- Weight
- Height
- Occupation
- Level of physical activity
- Dietary behaviour
- Smoking history

Any previous illnesses or surgery you've had in the past will also be noted, as will any ongoing medical conditions (like asthma or diabetes). The health of your parents and siblings is also important, as this can be an indicator for potential future problems.

Your doctor will be examining you from the minute you walk in the room (skilled observation can tell a lot about your health) and you should also have a full physical examination. This will involve

- Measuring your blood pressure
- Listening to your heart, lungs and possibly the arteries in your neck
- Feeling your neck, armpits and groin for enlarged glands
- Examining your skin surface for moles, or possible skin cancer
- Gentle prodding of your abdomen and examination of your testicles.

And then it's the all-important rectal examination. This takes 30 seconds, is mildly uncomfortable at worst, and may help diagnose a disease which kills nearly 1,000 of your countrymen every year. Get over your embarrassment!

You will probably also be sent to give a blood and urine test, and potentially bowel motion tests. The common measures here are your red blood count, fasting blood sugar, fasting cholesterol, prostate blood test (PSA) and kidney and liver function. A number of other tests can be added or performed later on the same blood sample if concerns arise, investigating things such as hormones, gout, thyroid, markers of a range of other conditions and antibody levels for diseases such as hepatitis.

By the time the doctor has gathered the information above, finished the examination and completed the laboratory request, you will have had time to ask questions and will have a picture of your current state of health. If there are some areas that need improvement, your doctor may give you some advice and tips to help you make positive changes to your lifestyle.

One of the most useful aspects of this session is for you to express your individual worries about your health. These concerns may be based on family experiences, your own previous health experience or your understanding (often misunderstanding) of common health problems you've witnessed in your friends of similar age.

And that's it! You're now good for the road for another year (but only if you have gained understanding of the maintenance work you need to do in the meantime).

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For more information on men's health visit www.you.org.nz

If you would like to know about the ins and outs of health insurance and the differences between different companies then give us a call strategi

KEY FINANCIAL DATA FOR 2011

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All data and information is current as at 1 January 2011 and subject to change and verification

Foreign Investment Fund (FIF) rules apply to

- If you hold a shareholding of less than 10% in a foreign company, foreign superannuation scheme, foreign life insurance policy or unit trust and it is an attributing interest
- If you hold a shareholding of more than 10% in a foreign company or unit trust and the CFC and the grey list rules don't apply.
- FIF investments held by an individual where the total cost is in excess of $50,000 at any time in that income year. There is a small range of trusts that also qualify for the $50,000 threshold (e.g. estates of a deceased person).
- FIF investments held by a company or trust.

AND in all cases none of the FIF exemptions listed below apply.

FIF rules exemptions

- Australian listed companies (shares on All Ords index, Australian resident which have a franking account). Refer to IR871 for list of exempt Australian shares. Staple securities do not qualify for Australian listed exemption.
- GPG (5 years from 2007/08 income year).
- **DE-MINIMIS EXEMPTION:** Interests in FIFs with a total original cost of less than NZ$50,000 (NZ$100,000 for a couple) at all times in that income year, if you are a resident individual investor or an eligible trust. Pay tax only on dividends received, unless the shares are held on revenue account.
- Shareholdings of 10% or more that come within the Controlled Foreign Company (CFC) rules for any type of investor. Passive income is attributed from a CFC that fails the active business test.
- Investments in Australian unit trusts that meet minimum investment turnover requirements or distributions and use the RWT proxy rules.
- Venture capital investments in grey list companies that were previously resident in New Zealand and maintain significant NZ presence.
- Offshore shares acquired through employee share purchase schemes in a grey list company if there are restrictions on the disposal of the shares. The exemption applies only for the duration of the restrictions.
- Shareholding of 10% or greater in grey list company and the person holding the interest is not a PIE, superannuation scheme, unit trust, life insurer, or a group investment fund.
- Specific exemptions for Australian regulated superannuation savings.
- Specific exemption for non-resident or transitional residents.
- Foreign exchange control exemption.
- New resident's accrued superannuation entitlement exemption.
- Non-resident's pension or annuity exemption.

- Refer to IRD website (http://www.ird.govt.nz/technical-tax/determinations/other/) for an up to date list of funds that have obtained an IRD determination as to which FIF calculation method applies to that particular product.

Independent Earner Rebate (from 1/4/10)

- Net income between $24,000 and $48,000 pa
- From 1 April 2009, $10 per week, abated at 13c per dollar above $44,000
- Not available to those receiving NZ superannuation, overseas pensions, other Government benefits and working for families tax credits.

Calculating FIF Income

Calculation method	Taxable income
Fair dividend rate (FDR)	= *(Opening Market Value at beginning of income year) x 5% + Quick Sale Adjustment* • Primary method to calculate tax on FIF unless investments prohibited from FDR rules • Tax is still payable if total return is a loss. However, individuals and family trusts can use the CV method to reduce tax liability. If the CV method gives rise to a tax loss, the loss is not recognised. • Tax is calculated on total FIF portfolio, excluding any investments prohibited from FDR.
Comparative value (CV)	= *(Closing Market Value + Gains) - (Opening Market Value + Costs)* • All realised and unrealised capital gains and income streams (e.g. dividends) are taxed • Losses can be claimed against other income unless the investments are also subject to FDR rules (see above where individuals and family trusts use CV method to calculate tax liability for their investments subject to FDR). • CV method applies to: – Foreign equities offering guaranteed or fixed rate returns; – Interest held in offshore entity which invests 80% or more by value in fixed rate shares or financial arrangements that are denominated in NZ dollars or hedged to NZ dollars.
Cost method	= *Opening Value x 5% + Quick Sales* • 4 different methods can be used to obtain opening value
Branch equivalent	= *(Branch equivalent income/loss) x (income interest)*
Accounting profits	= *(Accounting net profits/losses of FIF - foreign tax) x (income interest)*
Deemed rate of return	= *(Opening book value at end of previous income year) x deemed rate* • The deemed rate is set by Governor General for the income year.

Definitions

Foreign investment fund (FIF)	An offshore investment held by a NZ-resident taxpayer who holds: • Shares in a foreign company or units in a foreign unit trust; • An interest in a life insurance policy where a FIF is the insurer and the policy is not offered or entered into in NZ; • An interest in a foreign superannuation scheme. It does not include term deposits, bonds, debentures or money lent.
FIF income	Income derived from an attributing interest in a FIF, even though you may not have received any income at that point in time.
Attributing interests	• A direct income interest in a foreign company or unit trust, or • A right to benefit from a foreign superannuation scheme, either as a beneficiary or a member, or • A right to benefit from a life insurance policy where a certain foreign investment fund is the insurer and the policy was not offered or entered into in NZ. • No exemption applies.
Quick Sale Adjustment	Calculated when you both buy and sell attributing interest in the same FIF in the same income year.

Above you will find a table of financial data providing the current, as at 1 January 2011, Foreign Investment Fund (FIF) rules, exemptions, calculating FIF income, and definitions . We will include some others in our next newsletter in September.

Key Financial Data for 2011 reproduced with the permission of OnePath NZ Ltd.

You can never cross the ocean unless you have the courage to lose sight of the shore

Christopher Columbus

You are invited to
Fashion
&
Finance
Wednesday 17 August
5.30pm
At Wendys Boutique
11th Avenue Tauranga
Proceeds to Sweet Louise charity.
For more details please call Cathy 07 5715333 or email admin@g3freedom.co.nz

UK Pension Transfers - A Case Study

from Jane's desk (names have been changed to protect privacy and identity)

In spite of simplification of the rules around pensions in the UK back in 2006, there is still a vast range of pension types held by investors. These each have different, and often quite complex, structures. Deciding whether or not to bring your pension fund to New Zealand is by no means straightforward. There are a number of areas which need to be fully assessed before you have enough information to make an informed decision. For example, many pensions, and not just the larger company schemes, have some form of guarantee on all or part of the returns or guarantee you a level of income in retirement.

There are a number of other areas which need to be looked at and there are positives for leaving your investment overseas which include the tax free growth that the schemes provide.

It is important that you are aware of the ongoing fees you are paying - when no new monies are being added to an investment, these can have a significant negative impact. As an example, Helen came to see us recently. She provided us with as much information on her pension as she could. We sent off to the provider in the UK for the detailed facts required. Helen was surprised to find that her £4,000 investment had an annual management fee of 1.97% and an administration charge of £4 *per month*. The investment, therefore, needed to return 3.17% just to cover the charges **before** it started to give a return to her. We talked through her options and she decided the best thing for her circumstances was to bring her pension here. There are 6,533 company schemes in the UK which are members of the Pension Protection Fund. The main function of this fund is to provide compensation, usually when the company has suffered an insolvency event. Of these schemes 4,311 were in deficit at the end of May with an aggregate balance deficit of £13.5 billion. The scheme aims to safeguard up to 90% of a scheme member's entitlements.

At G3 Financial Freedom we make certain you are fully aware of the pros and cons before making a decision whether to transfer your pension entitlement to New Zealand. This involves an in-depth analysis of the fund and an examination of the advantages and disadvantages of transfer including tax implications. We then use comprehensive retirement modelling and planning to ensure the pension, wherever it sits, will do its job of meeting your longer term retirement needs and goals. We charge on an advice basis - so you pay us to review the pension properly, as opposed to only providing advice meeting the NZ requirements, as is often the case with NZ advice.

If you would like a review of your UK pension, please do give us a call - an initial consultation is free and without obligation.

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Goals + Guidance = Growth

G3 Financial Freedom Ltd - We Make Every Day Count

We are the financial advice company that can help you create the financial future you desire with peace of mind, security and confidence. We operate under the rules of the Financial Markets Authority and abide by the Financial Advisers Act 2008. We are voluntary members of the New Zealand Institute of Financial Advisers.
We are a group of Certified Financial Planners, Chartered Life Underwriters, Accredited Investment Fiduciaries and we are all Authorised Financial Advisers.
Talk to us about your financial future now. It is never to late to begin.

Left to right. Jane Benton, Tracey Coxhead, and seated, Charlene Overell and Gail Seddon