

October 2009 - March 2010

# PRIME Choice

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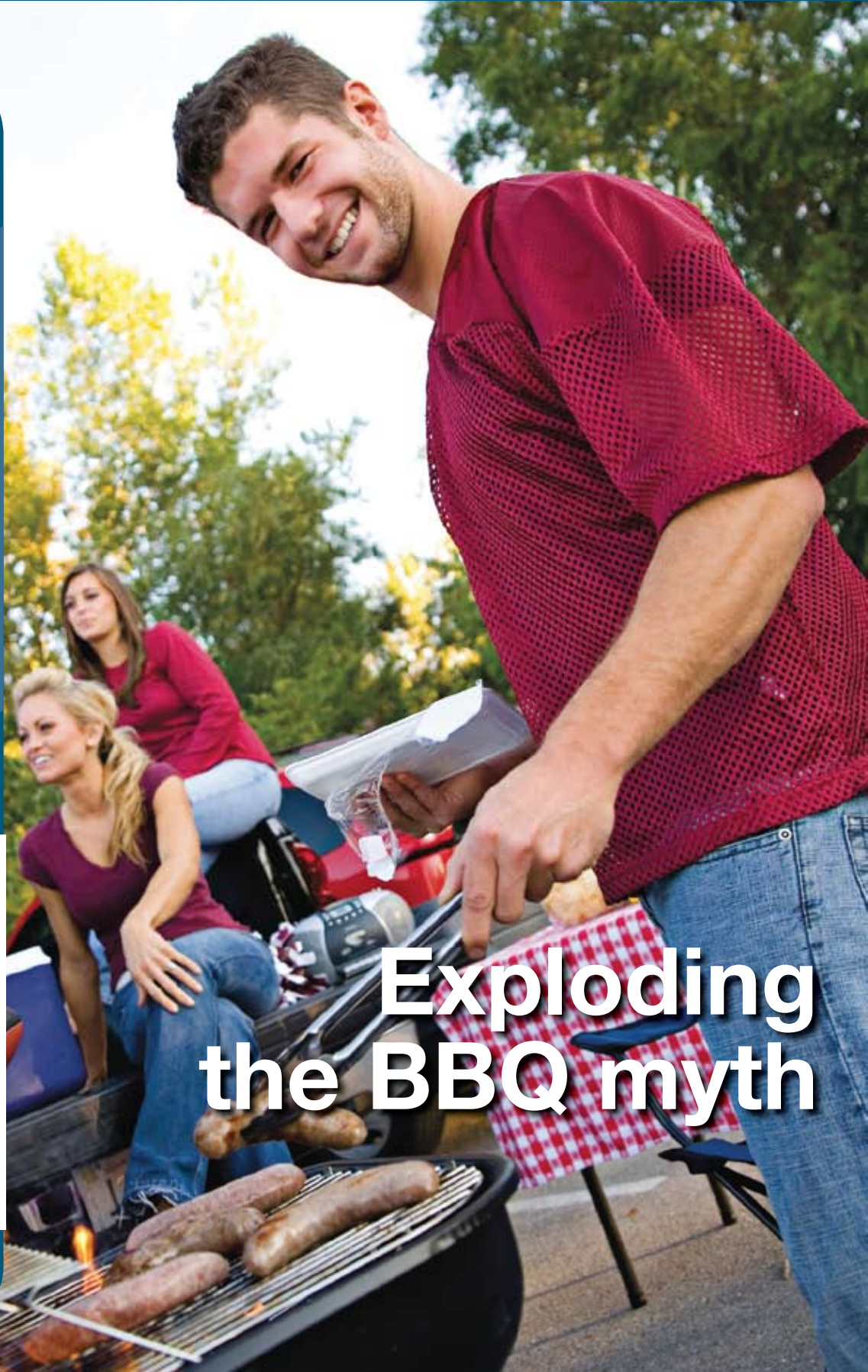


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# Exploding the BBQ myth

## Are you maximising your return on your most expensive business resource?

**If you analyse the financial statements of almost any business, you will find that salaries and wages is one of their biggest investments every year. When you add superannuation, workers compensation and payroll tax to this cost, it often equates to more than half of the business' total annual outlay.**

Unfortunately, many businesses fail to do the homework to ensure that they maximise the return on this major investment. Here's how to start working towards a more profitable result.



### **1. Determine the need, then match the resources - Don't create a need to fit the resources available.**

The key to efficient business is to have the right number and the right type of people for your business in the right roles.

First, decide what roles are required to make your business run like clockwork. Draw up the organisation chart that you would have if your business was operating perfectly, and determine the characteristics needed to successfully perform each position or role.

Compare the characteristics of your existing team members to the position they currently occupy.

- If they are a perfect match, avoid the temptation to promote them beyond their ability (great sales people usually don't make great sales managers) – look at alternative ways of incentivising them.

- If their personal characteristics don't fit their current role, move them either:
  - to another position that does require their particular characteristics, or
  - right out of the business – it's kinder for everyone in the long run

Perform targeted recruiting for any of the positions that can't be filled using the existing team members.

### **2. Ensure the whole team focuses on the things that drive your business**

It is critical that you understand what are the "key economic drivers" of your business, and then create systems to ensure the whole team focuses on those drivers.

For a manufacturing business, the key economic drivers may be

- Optimal quantities and costs of raw materials
- Efficient production process
- Efficient transport and delivery process

A service business is more likely to have the following key economic drivers:

- Efficient and courteous delivery of the service
- Repeat and/or expanded business from existing clients
- New Business generated by referrals from happy clients

Once you understand the key economic drivers of your business, you can design and implement reward systems for the team

members who achieve in those specific areas. That aligns the personal interests of each team member with the business interests and goals of the organisation. That in turn dramatically increases the chances of outstanding success for the business.

### **3. Take advice from your team**

Ask your team members for ideas on how to improve the way you do business, and implement the good ideas. There is nothing more motivating for employees than asking their opinion and acting upon their advice (and you'll be surprised how many good ideas you hear, if you ask). If the team has suggested a business improvement idea, they will encourage change and improvement in your business and will become an active part of the solution

### **4. Ensure the whole team knows what they have to do and how to do it.**

The most effective and motivated team members are those who understand what needs to be done and how it can best be achieved. Invest more into training and development and you will see the rewards.

### **5. Ensure the general environment is conducive to efficient performance**

Ensure your team have the right tools and equipment to perform their duties accurately and efficiently. Don't expect them to perform to their maximum if they have to work with poor quality equipment or in a poor quality environment.

### **6. Don't re-invent the wheel**

Prime Partners have extensive experience in determining the key economic drivers of business and in designing and implementing incentive programs that ensure your team is focused on the right inputs and outcomes. They also have the resources to help you review your overall HR program. If you want to maximise the return you are achieving from your workforce, contact us to see how we can help.

## Exploding the BBQ myth

**“I sold the investment property the other day” said Wayne as he flipped the sausages on the barbecue. “Got half a mill for it. Not bad for something I only paid \$200,000 for!”**

Wally was impressed, and inwardly berated himself for not having the courage to do what Wayne had done. He should have bought an investment property years ago and created wealth just like Wayne had done.

But should he? Is Wayne really being honest with himself? Let's look at the investment objectively. Wayne bought the property 10 years ago for \$200,000 – true. But Wayne has conveniently forgotten a few pertinent items:

- At the time of acquisition he paid stamp duty of \$5,490 on the purchase contract;
- He also paid \$2,000 to his solicitor to organise the purchase and the paperwork for the mortgage;
- He paid just over \$1,000 in loan application fees and mortgage registration costs;
- The real estate agent who sold the property charged him 2.5% of the selling price plus \$1,500 for advertising costs;
- And he had to pay his solicitor another \$1,500 to handle the sale of the property.

So the original cost of the property was actually \$208,490, and Wayne only received a net \$484,500 from the sale. Now the profit from the sale turns out to be \$276,010 - not the \$300,000 that Wayne is congratulating himself for.

But it gets worse. When Wayne completes his next tax return he will have to declare his \$276,010 capital gain and he will be taxable on half of it. If Wayne is earning \$80,000 from other sources, the capital gains tax on the sale will be \$59,172. That means Wayne's after-tax return on the sale will be reduced to \$216,838.

Still better than nothing you say? Well, let's have a look at what the property cost Wayne over the 10 years he owned it.

Because it was an investment property, and he had a reasonable amount of equity

in his home, Wayne was able to borrow 100% of the original purchase price of the investment property. He was smart enough to fix the interest rate for five years at the time he originally borrowed, and when the fixed rate period had expired, interest rates had fallen and he was lucky that the loan cost him interest at 7% virtually right throughout the period of the mortgage. Because the debt was tax deductible and because he still owed money on his home loan, Wayne had not been in a hurry to pay off the loan on the investment property, so he had made only the minimum payments on the 30 year loan he had taken out. Over the 10 years that he had owned the property Wayne had been charged total interest of \$131,287 and at the end of the 10 year period, he still owed \$171,615 on the mortgage.

Of course Wayne had received rent on the property, and had been diligent in increasing it by 5% every year. That had amounted to almost \$75,500 in total rent, but then the council rates, water rates insurance and maintenance on the property had set him back by \$23,500. So his net income (after interest and outgoings had amounted to minus \$79,287).

Naturally, he had claimed his negative gearing losses on his tax every year, and that had reduced his tax bills by a total of \$24,975.

So, overall how did he do? See the summary below. Almost \$191,000 generated for no original outlay? Well that's still OK isn't it?



Maybe not, when you consider:

- the potential risks involved. Wayne was lucky because he got his timing right. But if he had waited a little too long, the value of his property may have deteriorated significantly (due perhaps to the Global Financial Crisis and the resultant lack of confidence or simply due to the cessation of the First Home Owners Grant).
- the alternative results that could have been achieved by taking simpler, lower risk strategies. By contrast, if Wayne had simply increased his home mortgage payments by the amount he committed to the investment property, he would have reduced his home mortgage by \$230,355 at no risk and with no tax consequences. So even if Wayne does take the net cash that he generated from his investment and now pays it off from his home loan, **he will still be \$40,000 worse off than if he had simply committed the same cash flow to reducing his home mortgage!**

The moral is, don't be a Wally. Take your tax and investment advice from professionals, not from your mates around the barbecue (or from your butcher) – otherwise it may not just be your sausages that get burned!

### So, overall how did he do? Well here's the summary:

Net proceeds of sale (after agent's costs and legal fees)	\$484,500
Less: Capital Gains Tax on the sale	\$59,172
	<u>\$425,328</u>
Less: Cost of buying the property (legals, stamp duty & loan fees)	\$8,490
Total negative gearing losses over the 10 years	\$79,287
Less: reduction in taxes from claiming the negative gearing losses	\$(24,975)
	<u>\$62,802</u>
	<u>\$362,526</u>
Less: Payout of the mortgage on sale	\$171,615
<b>Net Cash generated from the investment</b>	<b><u>\$190,911</u></b>



## Got Debt? Follow these strategies and slash your interest cost

**Depending on your tax rate, the after-tax cost of non-deductible interest can be up to 86% more than the after-tax cost of deductible interest. That's why it is very much to your benefit to minimise your non-deductible interest and to ensure that as much of your debt as possible is tax-deductible.**

But if you have borrowed money for the home you live in, it clearly isn't tax deductible, so how can we achieve the aim of minimising non-deductible debt? Is it just a matter of paying off the non-deductible debt as quickly as possible?

The good news is that there are a number of legitimate strategies that can enable you to fairly rapidly convert non-deductible

debt into deductible debt and to achieve major savings in the after-tax cost of your interest.

### **1. Review your assets and re-organise your finances**

If you are one of the many people who made significant reductions in the loan over their original home, then decided to rent that original home out and buy yourself a new one (for which you would have borrowed significantly more), then you will find yourself in the position in which you are:

- Paying tax on the rent you receive,
- Getting only a minimal tax deduction on the interest charged on the reduced original mortgage, and
- Unable to claim a tax deduction for the

mortgage on your new home (because it was used to buy the house you now live in)

You will also be accruing a capital gains tax bill on the increase in value of the original home, because you can only be exempt from Capital Gains Tax on one home at a time.

**Strategy:** *Sell the original home and use the proceeds to pay out the mortgage on your new home. Then use the equity in the new home to purchase a new investment property. Providing the numbers work out correctly, you will have converted all of your debt into tax-deductible debt and you will have achieved a significantly improved after-tax result. Note that this strategy may involve triggering capital gains tax and incurring stamp duty and selling costs. It is important that all of the issues are taken into account before taking any action and we stress the need to check the details with your Prime Partners adviser before taking any action.*

### **2. Sell your business assets to a new entity**

If you are conducting business through a company or unit trust, or if you own a property that you conduct your business from, you may be able to re-structure your business and to use the funds released from the re-structure to pay out your personal mortgage.

**Strategy:**

*The key elements of this strategy are:*

- *Create a new entity that will purchase from you, the shares in your company or the real estate from which the business is being conducted;*
- *That new entity borrows from an external source to enable it to purchase your business asset;*
- *You receive the funds from the sale of the asset to the new entity and use those funds to pay out your non-deductible mortgage.*
- *The loan to the new entity has been used to purchase an income-producing asset, and the interest on the loan therefore becomes tax-deductible.*

There are added benefits to this strategy:

- Because you now no longer have a mortgage that you have to pay personally, you should be able to reduce your gross wages and replace those wages with dividends to the new entity. That could provide significant savings in Income Tax, Payroll Tax and Workers Compensation.
- The conversion of wages to dividends flowing to a new entity may permit the re-allocation of that income to family members on lower tax rates.
- The conversion of wages to dividends will mean that your business will be reporting higher profits which will make the business look more attractive to potential financiers and/or buyers
- If the new entity is a superannuation fund, and you have sold your business property to it, your business will then be able to pay a commercial rate of rent to the super fund. The rent will be tax-deductible to the business, and the super fund will pay a maximum of only 15% tax on that rent. If the super fund is paying a pension to the members (aged 55 or over), the rent could be tax-free to the super fund.

Warning! There are significant possible Capital Gains Tax, Stamp Duty and other implications involved in this type of re-

structure. We strongly urge you to obtain advice and a full costing of the strategy from your Prime Partners adviser before taking any action

### 3. Start debt-recycling

If you don't have a business or another property to sell, there is still a strategy which can be very effective in converting your non-deductible debt to deductible debt. This one is a longer-term strategy.

#### Strategy:

For this strategy, you will need to be prepared to maintain or increase your overall level of debt. The key elements are:

- Create a separate line of credit that you can borrow from to purchase investments. You will need to use your home as security for this loan so it's most efficient and cost-effective to have both loans provided by the one lender. It makes sense to review your existing loan at the same time and see if further savings can be achieved by organising the new finance package with a new lender.
- Commit as much of your ordinary income as possible to the repayment of your home loan
- Once or twice per year, determine by how much you have reduced the principal on your home mortgage by. Draw that amount out of your line of

credit facility and purchase appropriate investments with it.

- Ensure that the income from the investments is deposited direct into your home mortgage.
- As you build your investment portfolio, the income being deposited into your home mortgage will increase and your home mortgage will reduce at an increasing rate. Ensure you maintain your normal repayments on top of the investment income flowing into the home mortgage.
- Over a period of time, your home mortgage will reduce to nil, and your investment loan will rise to the original amount of your home mortgage. The differences will be:
  - your interest on the investment loan will be tax-deductible, and
  - you will have built an investment portfolio to the value of your debt or more.

Warning! The effectiveness of this strategy will depend on the interest rate you pay on your debt and the income and growth achieved on the investments you acquire. As with all of the above strategies, you will benefit from specific advice from your Prime Partners adviser and we encourage you to obtain that advice before proceeding.

you're invited to our  
FREE SEMINARS

### Transitioning to Retirement

Tuesday 20 October 2009 at 6.30pm  
Tuesday 9 March 2010 at 6.30pm

### Tax Planning & Tax Effective Investing

Wednesday 28 April 2010 at 6.30pm  
Tuesday 4 May 2010 at 7.00am  
Wednesday 12 May 2010 at 6.30pm

### Benefits of Self Managed Super Funds

Tuesday 17 November 2009 at 6.30pm  
Tuesday 9 February 2010 at 6.30pm

### What if things go wrong? Estate Planning & Family Protection

Wednesday 4 November 2009 at 6.30pm

**Where:**  
Prime Partners Boardroom  
Level 1, 230 Victoria Road, Gladesville

**Contact:**  
Virginia Bisoglio on 9879 7005 or  
email [service@primepartners.com.au](mailto:service@primepartners.com.au)

*Light refreshments will be provided.*

# Warning! Maximum Allowable Super Contributions Halved!

**Example:**

*Jake is on a \$109,000 salary package (made up of a \$100,000 salary plus 9% super).*

*Jake is under 50, and up to 30th June 2009, he had structured his package as follows:*

Superannuation Guarantee amount	9,000
Salary sacrifice contribution to super	41,000
Taxable wage	59,000
	<b>109,000</b>

*After 30th June 2009 (unless he turns 50, Jake will have to re-structure his package to a maximum of:*

Superannuation Guarantee amount	9,000
Salary sacrifice contribution to super	16,000
Taxable wage	84,000
	<b>109,000</b>

- the level of Medicare surcharge the may have to pay if their adjusted taxable income is more than \$70,000 (or their family's adjusted taxable income is more than \$140,000) AND they don't have private hospital cover
- their entitlement to a number of means-tested government benefits administered by Centrelink

If you have been using salary-sacrifice into super to avoid the more unpleasant aspects of the above issues, we're sorry to have to tell you that the strategy no longer works. If this was the only reason you were sacrificing into super, then it is time to re-assess.

And just to keep you fully informed, strategies such as:

- negative gearing into real estate or
  - negative gearing into other financial investments,
- are also added back to determine your Adjusted Taxable Income, so switching to these strategies will not restore the status quo.

If you are caught by these changes, there is now only a limited range of options available to you. As always, the team at Prime Partners are here to assist and we encourage you to contact Karen Parry at Prime Super Services or your Prime Partners adviser if you would like any advice on the above issues.



**In its most recent budget, the Rudd government halved the amount that can be contributed to superannuation as a deductible expense.**

If you will be :

- less than 50 by next 30th June, your maximum deductible contribution will now be only \$25,000 per annum and
- 50 or more by 30th June 2010, your maximum deductible contribution will be \$50,000

(the previous maximum deductions were \$50,000 and \$100,000 respectively)

**Revise salary packaging arrangements**

If you have been salary sacrificing into super up to the maximum amount (or amounts above the new limit), you will need to re-assess your packaging arrangements, because contributing amounts over the new limit could cost you 46.5% instead of 15% - and in extreme cases, these excess contributions could be taxed at 93%!

Note that the new limits apply to your total superannuation contributions, so you must take into account any contributions your employer is contributing as part of the Superannuation Guarantee obligations.

This will obviously have a significant impact on the amount of tax Jake will become liable for, as his taxable salary has increased from \$59,000 to \$84,000. Jake may have to consider alternative tax-planning strategies such as negative gearing in his own name or investment into other 100% deductible expenses such as forestry.

**Salary sacrifice no longer effective for taxable income planning**

At the same time as it introduced the halving of the deductible superannuation contributions, the Rudd Government almost made it compulsory for employers to report on their employees' PAYG Payment Summaries (Group Certificates) the amount of super contributed over the 9% statutory minimum.

Taxpayers who had been salary sacrificing into super will now have their salary-sacrificed contributions added back to determine their "Adjusted Taxable Incomes". This add-back will not increase their personal tax payable, but it will affect:

- the level of child support they are required to pay

## Redraw and Offset: A Step Ahead

**While interest rates remain low, it pays to stay ahead of your minimum monthly repayments by using a redraw facility or offset account.**

Since mortgage rates have dropped, nearly one in three suburban families continue to make more than the minimum required monthly home loan repayment\*, a choice that will save years off their mortgage and thousands of dollars in interest.

If you are able to do without the additional funds, you should resist the temptation

to reduce your mortgage payments and increase your personal expenditure. Mortgages with redraw facilities, and "interest offset" accounts offer convenient places to store money that you can still access for a rainy day. Either of these facilities provide you with the security of knowing you have a buffer to cope with hard times as well as the financial stability to weather any future interest rate rises.

Borrowers who are tempted to lower their repayments and put the money into a savings account should keep in mind:

- interest credited on savings is taxable and interest charged on the home mortgage is not.
- there is no risk involved in paying down your mortgage. Depending on where your savings go, there may be some risk of loss, and it is a fact of life that, the lower your risk on investments, the lower your return will be from that investment.

It is therefore much better to pay down your mortgage rather than accumulate interest-earning savings.

### **What is a redraw facility?**

It is a way of making additional repayments on your mortgage and then having access to this money again when you need it. Most home loan products feature a redraw facility, provided you are ahead of schedule with your repayments. Fees and conditions vary from one lender to the next.

### **What is an offset account?**

It is a savings account that is connected to your home loan. Instead of crediting you with interest on that offset account, the bank reduces the interest they charge on your mortgage. This provides a number of benefits:

- the savings in the offset account are available whenever and for whatever purpose you need them – no separate application is required to access the funds;
- because the bank is not crediting you with interest (but instead reducing the interest they charge on your mortgage), there is no tax payable on the interest
- the effective interest rate on an offset account can be substantially higher, because many of the banks simply charge interest on the combined balance of the mortgage less the amount in the offset account. These offset accounts therefore provide a tax-free return at the same interest rate as your mortgage – a much better return than you can achieve on most interest-earning investments.

Like redraw facilities, offset accounts differ in their fees, terms and conditions. Some are fully offset (100%) while others are only partially offset and may be conditional on a minimum account balance or withdrawal amount. Prime Partners can advise you of the suitability of different lenders' redraw and offset accounts. Contact us to discuss the best option for your needs.

\* May 2009 Mortgage Stress-O-Meter, Fujitsu Consulting.



## Looking for a vehicle for private or business use?

**With the government tax breaks currently on offer to small businesses, many owners are thinking about upgrading or replacing their passenger and light commercial vehicles. If you are thinking of purchasing a new motor vehicle, Prime Partners can help!**

Prime Partners Lending offers a car buying service through our trusted and reputable car buying service affiliates. Car buying service is the quick and easy way to arrange the purchase of your new motor vehicle. The car

buying service works for you to make buying a car hassle free with no heavy sales pitches, pushy car dealers or time consuming visits going from car yard to car yard. All you need to know is what type of car you are looking for and your budget. Our car buying service affiliates are committed to providing a friendly and efficient service that delivers a competitive price every time. Remember that the government's 50% "tax break" expires on 31 December 2009, so if you are in business, with gross revenue of less than \$2m per

annum, and in the market for a new car which will be used 50% or more for business purposes, now is the time to act!

If you have decided on your next new car and are looking for the best possible price from a premium car buying service contact Patrick Kazzi from Prime Partners Lending to discuss your need. Prime Partners Lending can also organise the financing arrangements for your new motor vehicle purchase.



## Prime Announcement

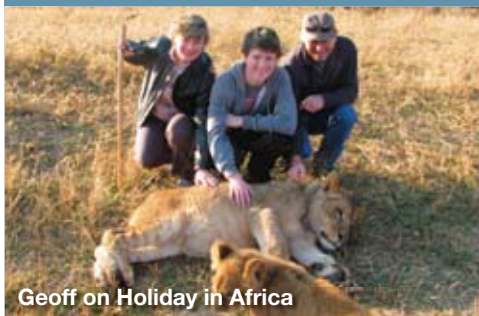


**John Stoel**

We are proud to announce that John Stoel has become a director and shareholder of Prime Partners. John has been with us for 4 years and many of you know him already. John has a number of passions in life. Unfortunately for him, one is the Canberra Raiders! The ones he is more successful with are the positive difference that he is able to make to his clients' lives through his expert knowledge and tailored advice.

John is a keen snow skier and has recently returned from a trip to New Zealand with all limbs intact (just!). If you have any questions in relation to John's areas of expertise (retirement planning, tax and business strategies, wealth accumulation and protection) or if you simply want tips to improve your snow-plough technique, John would love to take your call.

## Prime Partners News



**Geoff on Holiday in Africa**



**Financial Year Party**

On the home front, Prime Partners chose to celebrate the end of financial year on the 30th June 2009 at "Gladesville Sporties". The staff had lots of fun playing lawn bowls, snooker and other activities while also enjoying each others company and the hospitality of the club.

Whilst we were having fun on home soil, in recent ventures abroad, one of our directors, Geoff, with his wife Karen and son Patrick went on a family holiday to Africa. While making their way toward the Victoria Falls in Zimbabwe they had the fantastic opportunity to walk with lions.

Prime Partners would like to extend a warm welcome to our newest staff members. Luke Henderson and James Carey have joined our Accounting team and David Palmer has joined our Super team. We are delighted to have them all on board and look forward to the value that their respective knowledge and experience will bring to our business and our valued clients.

A big "Congratulations!" to James on his engagement to partner Samantha. We are pleased to be able to celebrate this memorable milestone with them and we wish the couple the best of luck as they prepare to begin a new life together.

## Dates to Remember

- 3 October**  
School Holidays begin (NSW)
- 4 October**  
Daylight Savings begins
- 5 October**  
Labour Day
- 18 October**  
School Holidays end (NSW)
- 21 October**  
Annual PAYG instalment due
- 28 October**
  - Quarter 1 (Jul – Sep 2009)
  - Quarterly BAS due
  - GST instalment due
  - PAYG instalment due
  - Superannuation guarantee contributions to be made
- 31 October**  
Due date for lodgment of annual income tax returns for individual self-preparers
- 31 October**  
Halloween
- 3 November**  
Melbourne Cup Day
- 11 November**  
Remembrance Day
- 19 December**  
School Holidays begin (NSW)
- 25 December**  
Christmas Day
- 26 December**  
Boxing Day
- 28 December**  
Boxing Day Holiday
- 1 January**  
New Year's Day
- 21 January**
  - Quarter 2 (Oct – Dec 2009)
  - Superannuation guarantee contributions to be made
- 26 January**  
Australia Day
- 26 January**  
School Holidays end (NSW)
- 14 February**  
Valentine's Day
- 28 February**
  - Quarter 2 (Oct – Dec 2009)
  - Quarterly BAS due
  - GST instalment due
  - PAYG instalment due

**For any assistance please contact Prime Partners on 02 9879 7005**