Financially Fit in 40 Days Challenge

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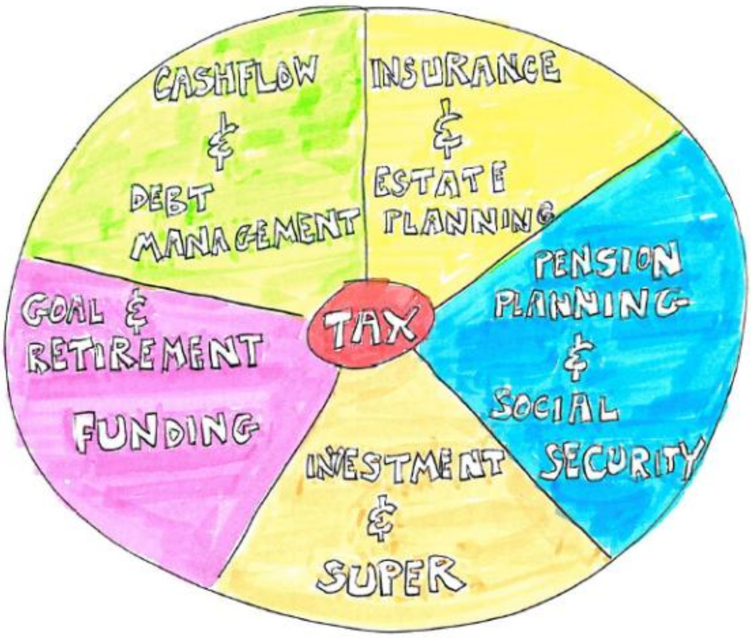
Continuing Your Action Plan Exercise: Week 5

Creating a Plan to Keep You Financially Fit…For Life

Last week you started building an action plan to get financially fit. Recall that there are six components – building blocks, if you like – to financial fitness:

- Cashflow and Debt fitness
- Goal and Retirement Funding fitness
- Investment and Superannuation fitness
- Pension and Social Security fitness
- Insurance and Estate Planning fitness
- Taxation fitness



Every single one of these components is an essential ingredient and they are all interrelated in some way. If you neglect any one of them then you put your entire financial house at risk.

The first and most important building block is **Cashflow and Debt Fitness** which you covered last week. If you have completed that week's exercises you have established your savings goals and have now put in place a strategy to direct your river of money in the direction you want, thereby achieving your goals. In this area of financial fitness you need to develop money handling ***habits***. However in the remaining five areas ***knowledge*** is what is going to make the difference for you.

But let's be realistic – you're not going to get a degree in social security, taxation, or superannuation here. Instead you're going to get on top of some enduring principles to guide you in each of these subjects, then ensure your action plan addresses all of those criteria.

We'll start with ...

Goal and Retirement Funding fitness

Guiding principles

Being financially fit in this area means you have:

1. a clear idea of the ***monthly cost*** your financial goals and your retirement will require
2. identified the ***specific investment assets*** that you intend are going to fund each of your goals plus your retirement
3. created an easy way of ***monitoring your progress*** towards the target

To achieve this you need to understand some key concepts like the time value of money, inflation, and future value versus present value.

Questions you must find the answers to:

- ☐ For each of my goals (refer to your goals worksheet from the goals exercise) I have determined that the cost of each goal in future value dollars is: *<insert future value here>*.
- ☐ Each of my goals is going to be achieved when the value of the following investment is equal to that figure: *<nominate here the investment earmarked for each goal>*
- ☐ In order to achieve that result, I am going to contribute the following each month to this investment: *<calculate here what monthly contribution required to achieve the outcome>*
- ☐ The investment needs to earn, after tax and after costs, an annual return of: *<calculate here the required annual net return of the investment>*

Each of these questions is an exercise in itself. However don't despair – help is at hand. With a little Googling you'll unearth not only sites that explain the concept of future value of money, but also you'll discover calculators to help you with the maths. You're going to learn that retirement is a very expensive business and that delaying your savings and investment program makes it vastly more expensive – financial planners and actuaries call it "the cost of delay". It's basically compound interest in reverse.

A great place to start is at a website called https://www.moneysmart.gov.au. It's run by the government and it's a new initiative designed to empower the consumer with facts about money. Bookmark it. It's superb.

Go to the 'tools and resources' drop down menu and select 'calculators and tools'. There is a retirement planner there as well as a savings goal calculator. Get busy so you can answer the questions above.

Guiding principles: Investment and Superannuation fitness

Guiding principles

Being financially fit in this area means:

1. Your super is fully funded and low-cost, with no valueless middle men.
2. Your investments, whether they be inside or outside of superannuation, are fat-free, globally diversified portfolios being managed according to an independently verifiable strategy that only takes risks bearing worthwhile rewards.

To accomplish this you need to calculate what your superannuation costs to manage and whether that's competitive. In addition you need an investment strategy that runs itself with maximum results for the effort, cost and risk.

Questions you must find the answers to:

- ☐ The admin fees in my super are: *<insert admin fees here as a percentage >.*
- ☐ The adviser fees in my super are: *<insert adviser fees here as a percentage >.*
- ☐ The investment fees in my super are: *<insert investment fees here as a percentage >.*
- ☐ The miscellaneous fees in my super are: *<insert miscellaneous fees here as a percentage >.*
- ☐ My investment strategy does not rely on a leap of faith because : *<explain how here>*

It's the satisfactory answers to those five questions that will ensure you're doing what you can in this area of finance.

The moneysmart website has a solid section on what to look for in superannuation; go to https://www.moneysmart.gov.au/superannuation-and-retirement/how-super-works/choosing-a-super-fund and have a read. On that page is a list of super comparison websites that you can have a look at to see where your fund weighs in.

Comparing super options boils down to this: fees. That's issue number one.

Issue number two is how the money should be invested. Unfortunately the financial services industry is full of misinformation and myth about this subject.

Basically you want to keep the costs to manage your super below 1% of funds invested, and you want to make sure you're not gambling with the capital of your hard won savings.

Let's get you off on the right foot ...

Open up your last super statement and check the fees you paid in the last financial year. Add them all up and divide them by the closing balance of the financial year. If the answer is greater than 1% then you've got some shopping to do: why are the costs so high?

It's very likely that the answer to the question is at least partially to do with your selected investment option: are you using an "active" investment approach or employing active fund managers?

"Be wary of the man who urges an action in which he himself incurs no risk." Joaquin Setanti

The world of investment philosophy is polarised: either you believe you can 'beat the market' by picking winners or timing when to get in and out of the market ... or you don't.

Regardless of which camp you're in, there is Nobel Prize winning research dating back fifty years now which verifies that one of these beliefs is proven, and one is unproven. Your task is to find out which one it is. Google it. You'll get the answer if you spend not much more than 30 minutes on it. It could be the most valuable half hourof due diligence you've ever undertaken. But that's all it will take. But before I release you on your quest, know this: there IS an answer. There is an independently verifiable investment strategy which, when diligently employed, ensures you only take risks that are worth taking, is reasonably cheap to deploy, and delivers you a much higher probability of achieving your goals **than any other approach**. Go.

Pension and Social Security fitness

Guiding principles

Being financially fit in this area means:

1. You have assessed your eligibility for Centrelink benefits and all available benefits have been applied for.
2. If you have a superannuation pension, it is structured effectively to minimize tax and maximize social security benefits.

The knowledge here is around income streams, taxation and Centrelink.

Questions you must find the answers to:

- ☐ The same questions you've answered for your superannuation apply to your self-funded pension fund. It's a cost and investment strategy issue. Answer these again here.
- ☐ You have made an appointment with a Financial Information Service (FIS) officer who has assessed your situation.

You see, Social security doesn't just provide for those who have fallen on hard times. There are often benefits that the average Australian is also entitled to. Not a bad explanation of social security here: https://www.moneysmart.gov.au/superannuation-and-retirement/income-sources-in-retirement/social-security.

Centerlink's Financial Information Services is excellent. You can make an appointment with a FIS officer and at no charge they will help you establish what benefits you should apply for and ways to maximise any benefits available for someone in your situation. The Financial Information Service is here: http://www.centrelink.gov.au/internet/internet.nsf/services/fis.htm. Browse that section for fact sheets and other resources to help you get what you're entitled to.

As far as pensions is concerned, the Australian Taxation Office has a surprisingly readable website devoted to the tax treatment of pensions. Honestly, there's no point attempting this unless you're brave; the other option is to visit a financial planner or accountant who can give you advice on whether you have the opportunity to structure a pension. Basically if you're 55+ then the option exists and you should get involved.

Either way, you need answers to those two questions to get yourself financially fit in Pension and Social Security.

Insurance and Estate Planning fitness

Guiding principles

Being financially fit in this area means:

1. You own comprehensive, low-cost financial protection that either has no commissions in the premium or the commissions are being rebated to you.
2. Your wills and powers of attorney are thoughtfully constructed, up to date, and are compatible with your tax entities and your super.

The learning curve here relates to how to mitigate the financial impact to your plans of events like premature death, disability or illness, as well as looking at protecting your wealth from unnecessary taxes or other hostile third parties for the benefit of those you care about.

Questions you must find the answers to:

- ☐ The commissions I am paying for my insurance advice are: *<$ here>.*
- ☐ My will considers life interests, testamentary trusts and nominates all my tax entities and was reviewed within the last 3 years for appropriateness: *<yes/no>.*

Is someone getting paid a commission out of your insurance premiums? Are you getting value for that because many aren't. Did you know that insurance companies can pay as much as 105% of your first year's premium out as a commission? Finding experienced and impartial advice in this area is possible but very difficult. Go to www.ifaaa.com.au to see just how scarce genuinely independent financial advisors are.

If you aren't getting any advice at all and your policy is paying out a commission then it's time to get busy on Google again. There are financial service companies who, for a flat fee, will sign on with your insurance company as your 'servicing agent' and will rebate to you the commission that your policy is paying, minus their fee.

Many people get wills that are utterly useless. This is because they bought one at the newsagency or because their lawyer gave them a stock-standard one without any advice. There are some key issues that you need to consider about what goes into your estate when you die; structure your assets to maintain maximum control, ensuring that the people you want to look after end up benefitting from your wealth, rather than some opportunist or, worse still, the tax man.

Also, a power of attorney is a document which empowers someone you trust to make decisions on your behalf when you're not able to. This subject is involved and so getting through it without a qualified professional requires a real commitment on your part. However a checklist to get you started is here: http://www.trust.com.au/documents/EstatePlanningChecklist.pdf

Taxation fitness

Guiding principles

Being financially fit in this area means:

1. Your returns are up to date and tax bills paid.
2. All available tax options have been considered so that your tax structures minimize your tax and protect the assets you are building.

The knowledge challenge here is around asset protection and tax minimisation.

Questions you must find the answers to:

- ☐ My average rate of tax is: *<insert rate as percentage of family income here>*.
- ☐ I have considered the value of incorporating trusts, partnerships, super funds and companies in my affairs within the last 12 months: *<yes/no>.*

Basically if you can get your average rate of tax in every year to between 20% and 30% of your gross family income then you're doing well and you're pretty fit here.

Unfortunately this area of finance is very similar to the previous one – getting fit here is about doing certain things every year. If you choose to go it alone without specialised professional guidance then you'd better be prepared to become that expert yourself. I can only direct you to the www.ato.gov.au which has a surprisingly good section on lodging tax returns, issues to consider in tax schemes that are being promoted during tax season, and calculators.