



# Financial Insight

## 2005

With compliments from your TOWER Adviser

Issue 6 Autumn 2005



## Welcome to the Autumn edition of Financial Insight

In this edition of the newsletter, we look at two very important subjects.

Firstly, we devote our lives to building our personal business assets – yet very few Australians take the time to consider the implications on their families and businesses should they be struck down with an unforeseen illness or injury. In many cases, the results can be catastrophic!

Secondly, a secure retirement or even an early retirement can be achieved – however it requires a defined strategy and the maximisation of personal savings if your goals are to be realised.

Through the Financial Insight newsletter we provide information that will help to de-mystify some of the complexities associated with financial services, income and lifestyle protection, wealth creation and the importance of setting strategies and achieving personal goals.

Of course, a consultation with your Professional Financial Services Adviser will supplement the information provided in this newsletter with detailed advice related to your individual circumstances.

If you would like any additional information on any topic covered in this and previous publications, please feel free to contact your Financial Adviser.

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## The Reality of Early Retirement

**An early retirement is usually on everyone's "wish list." A relaxing lifestyle in a warmer climate or the pursuit of a hobby or personal interest typically characterises the visions of what retirement is all about.**

Unfortunately, retiring later – not sooner – than anticipated, is becoming a fact of life. However, a select few are still managing to defy the norm and retire early.

You may be asking yourself, "How do they do it?"

The key is to take a proactive role in your retirement planning. Naturally, the sooner you begin planning, the more you increase your chances for early retirement.

Some retirees may require as much as 80 percent of their pre-retirement income to meet expenses and maintain their desired standard of living.

With the decline in the popularity of traditional pensions, people today are more and more responsible for funding their retirement.

### Redefining retirement

Many factors are redefining how people approach retirement.

Due to financial necessity, or sometimes just an overabundance of leisure time, some retirees are beginning to re-enter the workplace.

Many retired executives start their own part-time consulting businesses, others trade in their hectic 70-hour workweek for a type of pseudo-retirement, in which they work a lot less and spend more time with their families.

Part-time work during retirement can be an important income supplement, especially if you plan to retire early.

Another interesting factor changing the shape of retirement is that life expectancies are increasing. For some, spending one-third of their lives in retirement is a possibility.

Relying on retirement plans and government payments will be increasingly difficult because these retirement mechanisms were not designed to perpetually provide income.



Furthermore, as longevity has increased, over time, retirement plans have gradually shifted the savings responsibility to the individual. The pressure of building adequate retirement savings has been placed directly in the hands of a larger portion of the work force, who often must take initiative and contribute to their company sponsored retirement plans.

Your retirement assets, as well as your personal savings, will have to work longer and harder to help fulfill your personal objectives, regardless of whether you retire early or not.

An often overlooked aspect of planning is money management once retirement has begun.

To help ensure an adequate pool of retirement assets, your money will have to continue working

for you throughout your retirement years.

Inflation – along with the amount of income withdrawn from your retirement plan – will have a direct effect on how long you can live comfortably. Thus, personal savings will continue to be an overall part of your financial plan.

Budgetary constraints will also determine your retirement lifestyle. In order to better ascertain your financial picture, it is best to project what your retirement income and expenses will be.

Unfortunately, this process may be more difficult than it sounds. You will need to consider everything from greens fees at the local golf course to health insurance costs.

In addition, you will have to factor in inflation and how your income needs will change throughout the years.

For those who desire an early retirement, certain penalties may apply for early withdrawals from retirement plans. All options need to be studied and the consequences of any action taken should be reviewed by a qualified financial professional.

### It's your retirement: Be involved!

Today, early retirement is still a viable possibility.

Remaining on firm ground financially and working part-time, if necessary, have become integral parts of a successful retirement.

By maximising your personal savings to the best of your ability, you will increase your chances of reaching your retirement goals.

Remaining active and focused on attaining your retirement goals is particularly necessary if you are contemplating, or are forced into, early retirement.

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## A Lifetime of Building Assets Deserves a Few Minutes to Consider their Protection

### What are your assets?

When you think of the term 'assets' you most likely visualise possessions, such as your home and car, or perhaps you think of jewellery, savings or investments. As valuable as these are, a family's assets also include intangible objects that may not immediately be considered in dollar terms.

### What are your most important assets?

Once you broaden the definition of asset, the priority previously given to tangible assets may change. An easy way to determine the importance of your assets is to classify them into three categories.

### 1. Relational Assets

These are assets based on the relationships you have with the people closest to you and are characterised by a high degree of emotional and physical dependence or interdependence, such as:

- your spouse and their contribution as a breadwinner or homemaker;
- your children and their future potential;
- yourself and your contribution as a breadwinner or homemaker;
- other dependants, such as elderly parents; and
- children from a previous marriage.

## 2. Personal Assets

These are assets which have a quantifiable dollar value and which you identify as part of your personality, such as:

- your home;
- your motor vehicle; and
- your household possessions and valuables.

## 3. Financial Assets

These are items which hold financial value but which generally have no personal or emotional value, such as:

- superannuation;
- investment property; and
- shares, bonds and bank accounts.

### What value do you place on these assets?

One of the great ironies of financial planning and decision making is that we spend most of our time thinking, planning and worrying about financial and personal assets, and our relational assets rarely come into consideration.

### What about the 'volatility' of your assets

A characteristic of all asset types is volatility. The most common concerns regarding asset volatility are in relation to financial assets.

For example, a share portfolio is generally considered to be relatively volatile due to the ongoing possibility of gains and losses. These may amount to changes in value of ten, twenty or even thirty percent in a year.

However, the volatility of relational assets far exceeds this. 100% of a breadwinner or homemaker's dollar value can be totally lost at any time, through premature death and major illness or injury.

### What does this mean for you?

The high value and extreme potential for volatility of your relational assets makes them worthy of careful consideration.

While the protection of these assets may not be something that you have considered in the past, a few minutes spent calculating their worth may be the most financially powerful thing you ever do! The following list provides a good starting point.

### Protecting Relational Assets

- **Breadwinner(s)** – project income over the remainder of your working life, with some allowance for inflation.
- **Homemaker** – calculate a dollar value for the duties undertaken by the homemaker which would have to be paid for if they were no longer capable of performing these duties. This includes childcare, cleaning, transportation, cooking, home maintenance, accounting and laundry.
- **Children's potential** – for each child, calculate the funds required to allow completion of education



and any additional amounts required for tertiary study and realisation of their full potential.

- **Dependants** – how much will it cost to provide home and medical assistance for dependant relatives who may require independent care so that a surviving spouse is not left solely responsible?
- **Bequests** – do you have any relatives, charities or children from previous marriages who you want to provide for? If so, how much will this amount to?

### Protecting Personal Assets

- **Home** – how much debt remains on your home? Would you want this to be paid out?
- **Car and other possessions** – do you have personal loans and credit debts that would need to be paid?
- **Future plans** – are there any planned future purchases for major items such as a child's wedding that you want to provide for?

### Protecting Financial Assets

- You may have savings and investment goals that will be interrupted if you suffer from serious injury, illness or premature death? These may include large purchases such as a holiday home, boat or overseas vacation.  
Do you want to have to liquidate existing assets to provide an income stream? Would you like to allow funds for these goals to be immediately realised by a surviving spouse or dependant?

### Creating your asset protection program?

The value of your relational, personal and financial assets might be enormous, so what types of insurance can you put in place to create an 'asset

protection' program? There are four main categories of insurance which are designed to work together to provide security for you and your loved ones.

#### Life Insurance

This benefit provides a cash lump sum in the event of death. This can be paid directly to a beneficiary for immediate use in whichever way they see fit – there are no restrictions on what the money can be used for. Some life insurance policies also provide for an early payment if a terminal illness is diagnosed.

#### Total and Permanent Disability Insurance

This provides a lump sum if you suffer a major illness or injury that leaves you permanently incapacitated. The extent to which you must be incapacitated varies between insurance companies, but generally relates to a permanent inability to work.

There are often also provisions to allow payment in the event of particularly serious injuries such as loss of sight.

#### Trauma Insurance

Trauma insurance provides a cash lump sum upon diagnosis of certain medical conditions. While these may not be conditions that cause permanent disability or an inability to work, they generally require significant lifestyle changes, can involve exorbitant medical fees and include conditions such as heart attack, stroke and cancer.

#### Income Protection Insurance

There are a vast number of illnesses and injuries which have varying terms of impact.

These often fall outside the scope of total and permanent disability and trauma insurance. Income protection is designed to protect you from a loss of income due to such conditions by paying a replacement monthly income of up to 75% of gross income.

#### The next step

While this article provides a useful introduction to asset protection, a full analysis of your personal situation requires expert attention. Your insurance adviser can show you:

- how to accurately calculate your protection needs;
- how to build an integrated plan, combining the four types of protection; and
- how to source quality protection plans at an economical cost.

You don't have a choice about being exposed to these risks, but you do have a choice about protecting yourself and loved ones against unforeseen financial exposure.

## Ted and Jemima's Story

**While Ted and Jemima describe their lifestyle as comfortable, they don't consider themselves to be rich.**

They apply a monthly budget to their income and consider themselves to be financially responsible. However, when they decided to visit an insurance adviser earlier this year they received quite a surprise.

#### Ted & Jemima's Profile

- Ted is 42 and earns \$75,000 pa as a leagues club manager
- Jemima is 40 and earns \$35,000 pa working as a part-time sales consultant
- They have two children aged 5 and 7

#### Protecting their relational assets

Ted and Jemima determined that they would both prefer to continue working part time if either passed away, and so decided that they needed an insurance benefit to replace part of their income and to provide for a nanny.

- Their adviser calculated that to replace 60% of Ted's income for the next 15 years (until the children finished school) would require capital of \$675,000



- To replace 60% of Jemima's income would require \$315,000
- Hiring a nanny to perform basic home duties would cost approximately \$30,000 pa for the next 12 years and would amount to \$360,000
- They also wanted to establish an education fund of \$100,000 per child if either parent was to die

#### Protecting their personal assets

- Ted and Jemima would like to extinguish their \$220,000 mortgage in the event of either dying
- They have personal loans and credit card debts of \$15,000

#### Financial assets

- They are saving to buy a holiday house which they estimate would cost \$150,000

#### Their protection program

Ted's total protection needs amount to \$1,620,000 and Jemima's \$1,260,000. Their insurance adviser recommended they insure these amounts against death and total and permanent disablement.

She also recommended that they should each have trauma insurance to cover the cost of the mortgage plus one year's salary. This benefit would fund an extended period of leave without pay and provides a contingency fund for medical expenses, house renovations and rehabilitation.

Ted was also advised to insure his income for the maximum amount of \$4,687 per month.

## Did you Know/ Hints and Tips

### Did you Know

- A study conducted by the Australian Bureau of Statistics measured the economic value of typical household tasks. They calculated that such tasks would amount to approximately \$580 per week if performed by paid outside resources.<sup>1</sup>
- Males between the age of 30 and 65 have a 1 in 5 chance of dying before age 65 and a 1 in 6 chance of suffering a serious disability (of at least 6 months duration) before age 65. Females aged between 30 and 65 have a 1 in 7 chance of dying and a 1 in 4 chance of suffering a serious disability.<sup>2</sup>
- A child's education journey might cost anywhere between \$7,653 (without childcare) up to \$190,895 for a full time private education including a university degree.<sup>3</sup>

### Hints and tips

- Deciding who owns an insurance policy is an important decision. The person nominated as the owner of a life insurance policy receives benefit payments directly, without the need for distribution through a will.
- Check your employer superannuation policy to see if a death and disability benefit is provided. While this may not protect all of your needs, it should be taken into consideration when formulating your protection program.
- Some policies provide a cost saving by allowing you to combine multiple benefits under the one policy.

### Want more information?

Speak to your insurance adviser today to find out how you can protect your financial future. If you do not have an adviser please call Tower on **1800 226 364** or visit us at [www.toweraustralia.com.au](http://www.toweraustralia.com.au)

<sup>1</sup>. Australian Bureau of Statistics, *Unpaid Work and the Australian Economy 1997*, Canberra 2000.

<sup>2</sup>. Australian Institute of Health and Welfare

<sup>3</sup>. Carly Schwerdt, B. Vis Comm (Hon), B. Ed (Specialisation). *Why save for Education?*

