

**HOW TO DO IT**

**Make \$55,000 in six to eight weeks**

I recently purchased for a client a one-bed apartment with Sydney harbour views for \$515,000 which rented for \$350pw. Our client invested approximately \$50,000 in renovations, including project management fees, which took six to eight weeks.

The property valuation post-renovation was \$620,000 and the rent was increased to \$500pw. The interest on the \$50,000 renovation spend at 7.5% was \$3750pa.

- Total equity manufactured (after renovation costs): \$55,000.
- Increased rental return: \$150pw or \$7800pa.
- Increased cash flow (increased rental return less interest costs): \$77pw or \$4050pa.

**Note:** The holding costs will depend on the purchase price of the property, rental return and current financial position of the couple. The level of tax deductions will also vary depending on their income level.

As a rule of thumb, to have maximum control over the increased property value it is best to undertake the renovations shortly after purchasing the property. By doing this, the property will be revalued and sold in similar market conditions to the one in which it was bought, and removes the chance that the added value would be affected by a market decline.

The empty nesters will then be able to reinvest with a larger or similar budget if so inclined and repeat the process to achieve the \$50,000 target if it wasn't fully achieved from the first renovation project.

However, be careful with this strategy as if you sell within 12 months your capital gains tax bill will be twice as much as if you hold the property for more than 12 months.

**3. Buy, renovate and hold:**

A buy renovate and hold strategy is designed to increase the capital value of a property and give the option of borrowing against the increased equity created. In this case the property would be revalued after the renovation to determine the increased equity and then held as an investment property. Here, the empty nesters would also generate an improved rental return post-renovation.

As in scenario two, this approach is based on manufacturing capital value through renovation, rather than being solely reliant on market conditions. Another benefit of this strategy is that the empty nesters wouldn't pay the "out costs" such as capital gains tax, agent's fees and legal expenses which would be required when selling the property in scenario two.

Instead the couple could draw on the property's increased value and use that towards buying a second property. The couple then have the choice to sell the property and realise its capital growth at the height of a property cycle, or keep the rental income.

These strategies can be used in any market, however my advice is for property investors to stick to metropolitan areas. Capital cities have a large and varied employment base which means that they are not reliant on a handful of industries to be sustainable. The result is an ongoing supply of suitable tenants for a well-selected investment property.

If you are undertaking a renovation strategy, decide whether to manage the works yourself or appoint a project manager.

Out of the choices available, I recommend the buy, renovate and hold strategy for the empty nester couple as it gives them the ability to generate increased wealth without relying solely on market conditions.

In addition, they are able to use the increased equity in the renovated property to make additional investments without paying the costs associated with selling while also increasing their rental return.

If the empty nesters wanted to get really serious about increasing their wealth for retirement they could downsize now and use the leftover funds to invest in additional properties.

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# Retire on a high

**The pre-retirees** The aim of the couple who are near retirement is to increase their super by \$50,000 in five years. What are the strategies to get them there? They have \$350,000 in super (his \$200,000, hers \$150,000). She earns \$50,000 a year and he earns \$80,000.

**IT IS ACTUALLY VERY EASY TO** increase your super by \$50,000 in five years, given the tax benefits afforded to pre-retirees. Actually you can achieve this within two years. But if you want to continue your strategy for the full five years, you could more than double the amount, without having to live like a hermit. In fact, if we establish a transition to retirement income stream, or TRIS, for each member of the couple, over five years their super would be \$156,222 better off.

Unfortunately, the vast majority of those people for whom the TRIS is appropriate have not employed it, possibly because they don't understand it or know how to set it up. But I have seen very few people for whom this strategy does not have an immediate benefit.

Put simply, the TRIS is like salary sacrificing but with the added benefits of accessing funds inside superannuation. So how does it work?

Salary sacrifice is where you can put up to \$50,000 of your salary (for over 50s, or \$25,000 for under 50s) into superannuation and pay just 15% tax instead of your normal marginal rates.

The tax savings go towards your retirement benefit. You can't access your tax savings until you reach a condition of release which includes: retirement over age 55, age 65, transition to retirement, financial hardship, disablement etc. Effectively, your funds are locked up until you fully retire.

A transition to retirement income stream (TRIS) is a condition of release that allows a person aged 55 to 64 to draw between 4% and 10% of their superannuation account balance each year to subsidise their living costs while attempting to maximise their concessional contributions (15% tax) to super, thus reducing their normal income tax and increasing their



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	NO TRIS		TRIS	
Annual income	\$50,000	\$80,000	\$50,000	\$80,000
Super contribution (before tax)	-	-	\$13,000	\$43,000
Taxable income	\$50,000	\$80,000	\$37,000	\$37,000
Income tax	\$8550	\$17,550	\$4650	\$4650
Drawdown from super (year 1 <sup>1</sup> )			\$6000	\$8000
Cash flow, year 1	\$41,450	\$62,450	\$38,350	\$40,350
cash flow difference, year 1				-\$25,200
Starting super	\$150,000	\$200,000	\$150,000	\$200,000
Super guarantee (after tax)	\$3825	\$6120	\$2831	\$2831
Contribution after tax	-	-	\$11,050	\$36,550
Return @ 7%, first year (after tax)	\$8925	\$11,900	\$10,080	\$13,440
Total super, end year 5	\$233,919	\$318,168	\$252,743	\$455,567
Total super benefit, tris, end year 5				\$156,222

<sup>1</sup>Minimum withdrawal from income stream of 4%pa (tax free) increases as income stream super balance increases with investment return. With TRIS, super is split between an income stream, on which no tax is paid, and an accumulation stream into which the SG and before tax contribution is made.

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superannuation savings. (At age 65, you have reached a full condition of release so you no longer need a TRIS – an account-based pension is more appropriate and more flexible.)

A TRIS is like turbocharging your salary sacrifice because it allows you to put more into

superannuation, thus saving more tax, while drawing a little out to supplement your income (on a concessional tax basis). The higher your salary and your tax rate, the greater the benefit.

For example, our couple have \$350,000 in super and salaries of \$50,000 for her and

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\$80,000 for him. She should salary sacrifice at least \$13,000 a year, reducing her taxable income to \$37,000 (a lower tax bracket) and saving her \$3900 in income tax and boosting her super with a contribution of \$11,050 (after the 15% tax) each year.

For her, the TRIS is less effective as her super balance and salary are lower. In fact the difference for her over five years is just \$18,824, comparing the TRIS with doing nothing.

The husband on the other hand has a far greater benefit as his income and tax bracket are much higher. In his case I'd recommend contributing the full \$43,000 to his super fund (remembering to account for his employer's superannuation guarantee amount of 9% that legally is paid on the new income of \$37,000pa) thus reducing his taxable income to \$37,000, and paying \$11,600 (including super contributions tax) in tax instead of \$18,630 (including super contributions tax) – a saving of \$7031 a year.

Although his salary is reduced to \$37,000pa, remember that he can also draw back income from his super of \$8000pa (see table) to supplement this. The couple's after-tax income drops but is still a healthy \$78,700 a year.

If both partners chose to establish a TRIS, over five years they would have an extra \$156,222 in their combined super. They would be saving a combined \$9157 a year in tax and building their super for retirement.

If you are worried about your investments inside your super fund decreasing in value, thus reducing the benefit of a TRIS, do not stop the TRIS. The solution is simply to change to a more conservative investment option or even cash to maintain the tax savings benefit.

In terms of your mortgage repayments, if your taxable income remains above \$37,000, then you are better paying money into superannuation rather than paying the mortgage off. At retirement, you can then cash out money from your super to pay off the mortgage. **M**