



With the introduction of contribution caps, gearing has become increasingly important in the wealth accumulation and creation process for Self Managed Super Funds (SMSF). SMSFs are now able to enhance the potential for capital growth, increased dividend yields and franking credits through borrowing. With the right advice it may be possible to achieve your retirement goals sooner and improve the overall financial position of your SMSF.

The following case study is a hypothetical example only and uses rates and figures selected by Commonwealth Bank to illustrate how the Protected Loan works. The example should not be taken as personal advice or an indication of actual or future prices that may apply. It is not a recommendation to you to acquire either a Protected Loan under The Options and Lending Facility or the Securities referred to and should not be regarded as an accurate statement of affairs concerning any listed company.

Introducing Sue and David

Sue and David are both 45 years of age and have recently consolidated their superannuation assets to start the 'Sue and David Family Superannuation Account'. Their aim is to invest in assets which provide potential for capital growth.

The Strategy

Sue and David visit their financial planner to explore their available investment options. After discussing their situation and also carefully considering the fund's risk profile and time horizon, their adviser recommends a Protected Loan (PL) as part of an overall strategy.

As Sue and David believe that equity markets will rise over the next 5 years, they agree to a PL for \$100,000 with an LVR of 50%. This means that their SMSF will contribute \$50,000 with the balance of \$50,000 borrowed under the PL.

Importantly, the loan amount is protected on the maturity date, which means that there is no risk of losing the loan amount of \$50,000 at that time. A one-off protection premium of \$6,400 is payable at the start of the PL.

The \$100,000 is invested into STW, an ASX-listed Exchange Traded Fund which tracks the performance of the S&P/ASX 200 Index.

The terms of Sue and David's PL are:

Portfolio Value	\$100,000
Equity Contribution	\$50,000
Loan Amount	\$50,000
Loan to Valuation Ratio (LVR)	50%
Portfolio	STW
Protection premium paid in advance	\$5,706
Tax Rate of SMSF	15%
Term	5 years
Variable Interest Rate	7.66%
Estimated ATO Deductible Rate	9.40%
Net after tax benefit over term	\$3,443

The Result

Once the protection premium is paid, the SMSF will be required to pay interest at the variable rate of 7.66% p.a. on the Loan Amount of \$50,000 (estimated to be \$3,830 p.a. or \$19,150 over the 5 year term). In this case the SMSF will be able to offset a large portion of this expense against the assessable income of the fund.

To further offset the interest expense, the SMSF will receive estimated ordinary dividends and franking credits of \$29,900 over the term.

On an after tax basis, the strategy will produce a benefit of approximately \$3,443 to the 'Sue and David Family Superannuation Account'. This means that in this example the strategy is cash flow positive.

For a closer look at these calculations, please refer to the accompanying cashflows.

Creating long term wealth within super

The real benefit to Sue and David's fund will be any capital growth over the term. If STW rises in line with historical returns of 7.7% p.a.* over a five year term, the \$100,000 investment would be worth approximately \$145,000 in five years, representing a profit of \$45,000.

At maturity

At maturity, the fund can pay back the loan amount of \$50,000 out of its own funds and take delivery of the shares worth \$145,000.

Alternatively, the fund can instruct CBA to sell the shares and repay the loan. In this instance, CBA will pay back the initial equity contribution of \$50,000 as well as the \$45,000 profit to the fund.

In either case, the \$5,706 Protection premium which was paid in advance will be available as an offset to any capital gain in the fund.

Conclusion

By using a Protected Loan Sue and David's SMSF has gained exposure to a larger portfolio than otherwise possible. In addition, their SMSF has also benefited from:

- ➔ capital growth potential on a larger share portfolio
- ➔ income and potential tax benefits
- ➔ protection to the level of the loan amount
- ➔ no margin calls

*Source – Standard & Poor's. Returns are based on the S&P/ASX 200 Price Index rolling 5 year returns for the period from 1992 to 2010. Past performance is not a reliable indicator of future performance.

Important information

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Getting the right advice

As with any financial strategy, using a Protected Loan to borrow and invest is not without its risks. One of the key risks of using a Protected Loan is that your return could be negative, after taking into account the performance of your shares and borrowing costs over the term. That's why it's important to read the Product Disclosure Statement to ensure you are fully informed.

Speak to your Financial Adviser or call us on 1300 786 039 for more information about how you can create long term wealth within super.