WEALTH BITES 2024

JOHNSTON FINANCIAL

superannuation
investment
insurance
advice

What are investment bonds, and how could they be used?

Popular in the days before compulsory superannuation, investment bonds fell out of favour as super became the preferred tax-advantaged environment. With tighter restrictions on superannuation contribution limits and eligibility requirements, bonds might be worth a fresh look.

Investment bonds are a type of insurance policy primarily used as an investment vehicle. Available from a range of providers, investors can choose from a suite of underlying investments in much the same way as regular managed funds. Investment bonds shouldn't be confused with interest-paying government or corporate bonds. They are a unique type of asset offering a range of advantages.

Tax advantages

The primary attraction of investment bonds is that earnings are taxed in the hands of the issuing company at a rate of up to 30%. **Provided the bond is held for more than 10 years** and the 125% rule is not breached, no further tax is payable when the bond is cashed in.

While 30% is more than the 15% tax rate that applies to superannuation earnings, it is less than the current marginal tax rates that apply to people with an annual taxable income above $45,000. The higher your marginal tax rate, the more attractive investment bonds become.

Moreover, investment bonds don't lock up your money for the long term as super does. You can access your money whenever you like, but you need to be aware of some rules and tax implications.

If the bond is cashed out within eight years, all the growth in the value of the bond is included in your tax return. You will, however, receive a credit for the tax already paid by the issuing company. You won't be double-taxed.

Withdraw from a bond between eight and nine years, and two-thirds of the gain is declarable; and between nine and ten years, one-third of the gain goes into your tax return.

Bonds can be purchased with a single lump sum or with regular additions. However, to keep the original start date, an annual contribution cannot exceed 125% of the previous year's contribution. If it does, the clock starts again for the 10-year rule. Another option is to simply purchase a new bond.

Additional benefits

Insurance bonds can be useful estate planning tools. As a form of life insurance, if the owner dies, the proceeds will be paid directly to nominated beneficiaries. The money doesn't go through the estate and can be paid out quickly. In addition, the proceeds are not taxable in the hands of the beneficiaries, even if the bond is less than 10 years old. Allowing for relevant tax rates, they may also be a good vehicle for saving for a child's education or other long-term goal.

Timing

Due to their long-term nature, it isn't just your current marginal tax rate that is important; it's what your rate will be in the future. As many retirees pay little or no tax, particular consideration must be given to purchasing a bond that will be held until after retirement.

Suitability

Investment bonds aren't for everyone, but they may suit investors who:

- have reached their contribution caps for super contributions or are no longer eligible to contribute to super due to age;
- do not wish to lock away their money in super;
- are saving for a long-term goal and have a marginal tax rate above 30%;
- have specific estate planning needs.

There is much more about investment bonds than we can cover here. As with any type of investing, there are risks involved with bonds, and these must be taken into account.

Contact us if you would like to learn more about how investment bonds could be part of your investment portfolio.

Johnston Financial Pty Limited

170 Bridge Street – Tamworth – NSW 2340

02 67668211

advice@johnstonfinancial.com.au **www.johnstonfinancial.com.au**