Couples divided on when to retire

KATHLEEN A. HUGHES

LET'S say you have managed to stay married by the time you hit middle age. Get ready for one more marital hurdle.

The odds are your spouse won't feel the same way you do about when to retire. A recent study by Fidelity Investments found that 62 per cent of couples disagree on the timing of their respective retirements.

Consider Deborah Ewing, a 55-year-old lawyer, and her husband, Patrick Hickey, 62, a tax-software programmer.

Hickey has a two-hour-plus daily commute from their home to work in Los Angeles and says he feels tired. He would like to retire "as soon as possible".

No go. "I have told him he has to stay working until the last kid is out of college in four years," Ewing says. "For me it would be annoying not to have someone pulling their weight. I realise he's older. But on a personal level, I don't see it as positive. My perspective is he would potter around the house."

Having watched her father retire, she also thinks it's healthier to keep working. "I think when people retire they slow way down and become less productive, less interesting, less healthy, less financially robust," Ewing says. "I plan to work as long as I can."

Hickey sees it differently. "Her perspective is a little bit warped," he says. "She sees me riding in the saddle until the very last day when I drop from the saddle. My body feels the way it feels. She can't really know how I feel and function."

So the debate is at a standstill, at least for now. "She is worried that I will quit too soon and start having fun and we won't have sufficient funds," Hickey says. "There may come a point when I retire even if she doesn't want me to."

The days when a husband retires at 65 with a corporate pension and his wife follows him to a golf course in Florida are over. Most women approaching retirement age are now working, and many have their own retirement savings and viewpoints.

"Many women have entered the workforce later and are at their peak when men slow down and want out," says Dorian Mintzer, co-author of *The Couple's Retirement Puzzle*. "The timing can create some struggles," she says.

Only about half of couples retire within two years of each other, says Richard Johnson, a senior research analyst at the Urban Institute, a social policy think tank in Washington, DC.

Men approaching retirement age are, on average, almost four years older than their spouses, he says. And the larger the age difference, the less likely they are to retire at the same time.

"There's a lot more for a couple to negotiate now," says Maximiliane Szinovacz, a professor of gerontology at the University of Massachusetts Boston.

"It's no longer one retirement and one drastic transition." Indeed, some negotiations seem to go on and on, since many baby boomers expect to work longer and retire gradually, taking on a series of jobs or part-time work.

Therapists stress the importance of planning, clear communication and compromise.

"In order for it to work well, each person needs to clarify their own vision of what's important and learn to talk with each other," says Mintzer, the author, who is also a retirement coach.

"Sometimes it's agreeing to disagree," she adds.

THE WALL STREET JOURNAL.

Defence Housing investors are sitting pretty, say experts

Industry figures have leapt to the defence of the accommodation provider

ANDREW MAIN

DEFENDERS of property agency Defence Housing Australia have come out swinging following criticisms last week in an article by Melbourne property specialist Monique Wakelin, who claimed asset capital growth might be affected because most of the properties had been built in low land-value areas.

DHA has about 19,000 properties under management with a value of about $10 billion, sprinkled around Australia in capital cities and around military installations, on long-term leases to mostly private investors.

Tim Coates, a director and head of property at Dixon Advisory, said DHA was a good vehicle for investors who wanted to "set and forget" in terms of a property investment, rather than being involved hands-on and regularly.

"For a client looking for a long-term, low-risk investment with repairs and maintenance paid for, it's a worthwhile proposition," he said. "It depends on how involved the client wants to be. The guaranteed rental floor allows you to know what the rent will be for the next 10 to 15 years."

DHA charges 16.5 per cent for property management and maintenance on the properties it sells, with the inclusion of a repaint at the end of the lease, which usually runs for between 12 and 15 years. That's about twice the 8 per cent most agents charge for collecting rents but involves a significantly higher level of service, covering regular maintenance as well as the repaint at the lease's expiry.

Asked about the location issue, Mr Coates said: "With DHA and any other property asset, you have to be very comfortable with the geographical location and the asset type. I think DHA have a vast portfolio, some on growth areas and some not, and investors have to be aware of that."

Another observation in the article, that you can only sell the property to another investor during the life of a lease, "which means home buyers who represent 70 per cent of the market are excluded", drew a strong response from Tony Winterbottom, DHA's general manager sales and marketing.

"There are very few DHA properties that are sold during the lease," he said, "and it's well known that if you sell a house that's leased, you are selling with the lease attached."

Mr Winterbottom said more than 50 per cent of houses subject to sale and lease-back arrangements were re-leased when the lease expired, at which point the owners were free to do what they wanted with the houses, which he said were "salt and peppered" or sprinkled around conventionally owned houses in suburbs to avoid clustering military staff.

He rejected any suggestion that DHA buys or builds houses of lower value than others nearby.

"DHA as a property developer and buyer is well regarded and we often get premium selection on new developments," he said. "That allows us to buy in very good locations around the country."

Mr Winterbottom said many DHA properties were close to the centre of major cities and named the Sydney suburbs of Caringbah, Eastwood, Ermington, Kellyville, Kensington, Killara, Little Bay and Miranda as locations where DHA manages properties. "We're not talking about houses in the middle of Woop-Woop," he said.

On the issue of the 16.5 per cent running charge levied on investor-owned DHA houses, he cited a 2007 report by Access Economics. It concluded that after factoring in the extra maintenance services and rental guarantee provided by DHA, "what was found was that under a broad range of scenarios, once these costs are accounted for, DHA investors face lower costs than if they had leased through a traditional rental agency".

The study concluded that over a nine-year lease, a DHA investor would make at the very least a saving of about $423 a year by avoiding, say, $1413 of repair and maintenance bills. If the bill were at the top end of expectations, say $3225, the investor would save $4600, even if gross rents were identical at $23,480 a year.

Stuart Nisbett, managing director of advisory group Archerfield Capital, said he had advised DHA and potential buyers in the past and had found DHA "highly ethical" in its dealings.

He disputed the suggestion that DHA properties were overpriced, noting that when he had had valuations done "some came in under the DHA valuation, and some came in over".

He conceded he had dealt with properties only in the deeper markets of Sydney, Canberra and Melbourne but said that DHA was well aware of price trends in different suburbs and set its prices "at the market".

Of the 16.5 per cent fees, he said: "The fees look high but they cover a great deal more than conventional agent's fees and DHA acts as the tenants' representative, making sure that the properties are correctly maintained."

A DHA investor would save at least $423 a year

A house built by Defence Housing Australia in Cairns in far north Queensland

Comparison of the DHA management fee model versus traditional real estate agent fees

AVERAGE ANNUAL COSTS OVER A TYPICAL NINE-YEAR DHA LEASE, 2007 DOLLARS

WEEKLY RENT: $450 ■ DWELLING TYPE: HOUSE

DHA model	Average per year
Gross rent per annum (52.18 wks)	$23,480
LESS	
Management fees at 16.5%	$3874
PLUS	
Benefit of rent floor (removes risk of rent reducing below 1st year rent)	-27
TOTAL costs, $ per annum	**$3847**
TOTAL costs, % of gross rent	**16.4%**
Net rent per annum (over 9 yrs)	**$19,633**

Traditional model	Average per year	High per year	Low per year
Gross rent per annum (52.18 wks)	$23,480	$23,480	$23,480
LESS			
Management fees (varies by agent)	$1878	$1996	$1761
Vacancy costs (varies over time)	$450	$675	$225
Letting fee (varies by agent)	$675	$900	$450
Other agent fees (varies by agent)	$200	$300	$100
Repairs (not included in agent fee)	$2319	$3225	$1413
Painting (not included in agent fee)	$303	$416	$189
Carpeting (not included in agent fee)	$244	$355	$133
Hassle/owner's time/input	$306	$613	$0
TOTAL costs, $ per annum	**$6375**	**$8480**	**$4270**
TOTAL costs, % of gross rent	**27.2%**	**36.1%**	**18.2%**
Net rent per annum (over 9 yrs)	**$17,105**	**$15,001**	**$19,210**
DHA SAVING $ per year	**$2528**	**$4632**	**$423**

Source: Access Economics

Play it safe by adding custard

ROGER MONTGOMERY

PUDDING and custard. At this time of year, there are no two food combinations I am less resistant to. For me, all investing is like pudding and custard: two ingredients that must be combined. In investing, it's quality and value.

Regular readers of this column will know that quite often I focus on the attributes that constitute an extraordinary business. That's the quality. But there are two parts to the investing equation: quality and value.

Identifying the best stocks is half the challenge and buying them for less than they are worth is the other half. In all investment decisions the margin of safety will determine the return. Although a company may have stunning fundamentals, the decision to invest should be made only when the company's share price is trading at a steep discount to its intrinsic value. This way, investors will mitigate some of the risks while ensuring their exposure to potential profit is maximised.

Let me illustrate the point using Austbrokers, which manages a network of insurance brokerage and underwriting businesses. Since 1985, management has employed a stable business model that has led to organic growth and involved acquisitions. This strategy is well suited to the insurance industry.

Historically, Austbrokers' earnings have grown at 15 per cent a year even though most of the earnings from previous years are paid out as dividends and shareholders have not been required to stump up further capital. The company is net cash positive, although it maintains a conservative level of debt on the balance sheet to fund acquisitions.

Austbrokers has all the trademarks of a quality business but this does not necessarily make it a wise investment. The company may get a tick for quality, but are its shares trading at a sufficient discount to intrinsic value? According to Skaffold.com, intrinsic value for this business has been growing at about 12 per cent since 2007 but the share price is now 28 per cent above its value. There is no margin of safety.

Even if I look at conventional measures we can get a sense of the diminished margin of safety. In 2009, the share price was 12.5 times Austbrokers' earnings per share, while this year its share price has been trading at more than 17 times its earnings per share. The multiple of earnings investors are willing to pay has grown 50 per cent in just three years. It is reasonable to conclude the recent share price rally has extinguished much or, if not, all of the value.

At Montgomery we always rely on a margin of safety, and so should you. A conservative margin of safety will protect you when your estimate of a company's intrinsic value is too optimistic. It will minimise your exposure to a fall in the company's earnings and can turbo-boost your returns. For more about margin of safety, pick up a copy of *Value.able* for Christmas.

There are two essential ingredients to a happy Christmas dinner and the investing equation, and at this time of year I can't resist the combination.

Roger Montgomery is the founder of Montgomery Investment Management and the author of Value.able: How to Value the Best Stocks and Buy Them for Less Than They're Worth, available at www.rogermontgomery.com.

US property and currency play worth a look for those chasing yield in big caps

IAN VERRENDER

THEY seek it here. They seek it there. After three years of range trading and with the local bourse still sitting at about two-thirds of its 2007 peak, equity investors who were content to sit on cash and reap attractive interest rates have been forced back into the market in recent months.

While most are still wary of any serious prospect of capital gains, given the global uncertainty, they've been hunting for yield to replace those once attractive term deposit rates. The hunt is rapidly becoming an obsession.

The obvious targets, such as the big four banks and Telstra, have benefited handsomely since mid-year and helped to power a run on the local market. But investors have begun to cast a wider net in an effort to diversify as the potential for gains in the banking sector is limited by the recent uptick. In recent weeks, several new offers have been launched in a bid to cash in on the yield quest.

A relatively forgotten equity instrument, the listed investment company, has consistently outperformed the broader stockmarket for decades. And studies here and in the US point to advantages LICs have over unlisted funds that have helped them deliver far better returns for investors.

As a sector, LICs have focused on delivering yield, usually via fully franked dividends. In mid-November, several new yield plays hit the market in an attempt to woo investors back towards LIC-type structures, including Dixon Advisory's US Masters Residential Property Fund.

While it is more correctly called a property fund rather than an LIC, this is a listed closed-end fund with a stable amount of capital to invest. Like all LICs, it is not forced to sell assets if unitholders want to redeem their units. It simply sells them to other investors via the Australian Securities Exchange.

The US Masters Residential Property Fund has been formed specifically to cash in on two historical market anomalies: the incredible strength of the Australian dollar and the stunning decline in American residential real estate.

It owns 430 houses and 948 units in and around New York City, with the houses predominantly in Hudson County, New Jersey, and apartment blocks in Brooklyn and Harlem.

This week the fund closed an issue seeking to raise a minimum of $40 million, and up to $80m, adding to the $165m it has already raised and invested.

It is paying a 6.4 per cent yield with a 10c dividend on its $1.56 share price, and plans to continue that payment. Crucially, its net tangible assets remain at $150.6m while its stockmarket valuation sits above $162m.

Chief executive Alan Dixon, who lives in New Jersey, said last month the fund aimed to take advantage of the dramatic downturn in US housing, not high-end penthouse apartments. The strategy, he said, was to focus on a market segment that was below the threshold of large institutions but beyond the financial scope of individual investors.

US property prices are likely to remain depressed for some time. The US housing market collapse forced many homeowners to abandon their properties. Unlike Australia, there is little if any recourse for the bank to pursue them. But with a bad credit history, the former owners are banned from taking out new housing finance for several years, limiting any sudden resurgence in demand. That has forced many to rent. As a result, rents now are significantly higher than mortgage repayments, delivering remarkable yields on the funds invested.

That market distortion will work itself out over time. But as it does, investors hope property prices will rise, delivering capital gain to the fund. A revaluation of the US Masters portfolio currently under way suggests that already has begun.

Unlike many LICs, the US Masters Property Fund trades at a slight premium to net tangible assets, but volumes have been very low. That may improve with the extra units issued.

The fund has taken no hedging on the portfolio, hoping to capitalise on an improved greenback in the future or an easing in the Australian dollar. While in ordinary times that strategy could be considered high risk, few analysts or economists believe the Australian dollar can sustain its current levels in the long term.

For those hunting exclusively in the large cap pool for yield, this property and currency play could complement the portfolio and may be worth a look.

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Self-managed superannuation funds can borrow to buy assets, but it pays to know the rules

MONICA RULE

LAST week, we examined the pitfalls of self-managed super funds borrowing money to buy assets. This week we will cover some examples. Property that is under a limited recourse borrowing arrangement (LRBA) can be repaired and maintained using the borrowed money, but it cannot be replaced or improved. However, you can use other money in your SMSF to replace or improve the property as long as it does not become a different asset.

For example, your SMSF can borrow to buy a house with broken windows then use some of the borrowed money to repair the windows. This is a repair.

However, your SMSF cannot purchase a rundown house and then substantially renovate the house. This is an improvement and cannot be financed under the LRBA.

If your SMSF restored a kitchen following a fire, the restoration is a repair, but if the kitchen was extended to increase its size, the extension is an improvement. Adding a dishwasher to the kitchen, however, would not be an improvement, even if it was not previously part of the kitchen. This is because the dishwasher would be treated as a minor improvement to the state of the asset as a whole.

The asset must be replaced like-for-like. If a three-bedroom house is destroyed and replaced by a four-bedroom house that is not a like-for-like replacement. However, if the funds to rebuild are from an insurance company and not from the LRBA then it is OK to do this. If superior materials or appliances were used for repairs, then it is a question of degree as to whether the changes improve the state of the asset as a whole.

If alterations are made that fundamentally change the character of the asset and the proprietary rights, this makes the asset a different asset.

Other money, whether from your SMSF or elsewhere (for example, insurance), can be used for improvements as long as the improvements do not make the asset a different asset.

If a house is demolished, following a fire, and replaced by three strata titled units, the asset becomes a different asset. The character of the asset has fundamentally changed along with the proprietary rights, as the alteration has created three different assets. Another example would be a residential house being converted into a restaurant, which includes fitting out a commercial kitchen. The character of the asset has fundamentally changed from residential premises to restaurant premises. This is a different asset.

Improvements such as an extension, adding a swimming pool, extending an outdoor entertainment area, adding a garage and driveway or even adding a granny flat would not change the asset. These alterations are acceptable as the changes do not fundamentally change the character of the asset. As long as the SMSF uses money from elsewhere and not from the LRBA, these improvements are OK.

The law does not restrict from whom an SMSF may borrow

Some lenders may request a member of the SMSF to act as a guarantor for the LRBA. This is acceptable, but members need to understand what the lender will do if the SMSF defaults on the loan as any payment made by members to the lender to repay the loan could be treated by the Tax Office as a personal contribution. This contribution, when added to other contributions, could exceed their contributions limits.

Members must ensure that the lender seeks repayment first by seizing the asset acquired under the LRBA before exercising its right to call on the members for any shortfall on the outstanding loan. After seizing the asset, any shortfall amount paid by the members to the lender would not be considered a contribution.

Trustees also cannot enter into an LRBA for assets already owned by their SMSF. This means money cannot be borrowed under a LRBA to fund repairs for assets already owned by the SMSF.

There are no restrictions on your SMSF purchasing assets from an unrelated party. However, if the SMSF wishes to purchase assets owned by members of the SMSF or other related parties then the only types of assets that can be acquired under a LRBA are listed securities (for example, shares listed on the stock exchange) and business property (land and buildings used exclusively in a business).

A common error occurs where SMSFs enter into a LRBA to purchase residential property from a member, which is not allowed.

Superannuation law does not restrict from whom an SMSF may borrow. Therefore, the SMSF can enter into a LRBA by borrowing from a related party (including a member).

However, as the law requires all transactions be conducted at arm's length, the terms of the loan, calculation of the interest rate, frequency of the interest repayments, the obligation and timing of principal repayments, and the security offered for the loan must all be at commercial, arm's-length terms.

Banks and other financial institutions are learning about this law as well, so may not be aware of all the requirements. It is important for trustees of SMSFs to understand the borrowing law so penalties can be avoided.

Monica Rule is the author of The Self Managed Super Handbook — Superannuation Law for Self Managed Superannuation Funds in plain English.
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