Build on a brave start

Susan Hely hears about a caring community

NAMES: Gavin & Rebecca Stammers
STATUS: Married couple, one daughter
QUESTION: What should we do with our daughter's money until she is 18?
SOLUTION: A term deposit. To rev up return, invest part of it in shares yielding high dividends.

When two-year-old Megan Stammers was diagnosed with leukaemia in 2010, the 3000-strong community of Blayney in western NSW went all out to raise funds, with raffles, auctions and head shaving for sponsorship.

The Stammers family relocated to Westmead children's hospital for eight months while Megan had chemotherapy. Gavin's employer allowed him to transfer from Orange to work in Sydney. The family stayed in the supportive Ronald McDonald House, adjacent to the hospital, which is for families who live more than 100 kilometres away. Rebecca often slept on a rollaway bed in Megan's room.

Blayney raised $32,000. "It was overwhelming," says Rebecca. "We live in a close-knit community. It's the way people pull together."

The money sits in Megan's CBA Youthsaver account, set up when she was a baby. The Stammers are happy with the account, which has bonus interest of 4.75%pa, on top of 0.01%pa, each month a deposit is made, if there are no withdrawals.

They would like to put the money aside for her when she turns 18 but ponder the best investment. They bought their house two years ago and have been advised to use their mortgage offset account, but they would like to keep the money separate for Megan. They have super with First State Super (Gavin) and Local Government Super's defined benefit plan (Rebecca). Twenty years ago Gavin started a savings plan. He puts in around $2200 a year and pays fees of $360 ($146 on a policy contribution fee and $215 for insurance).

Susan Hely was a senior writer on investment at The Sydney Morning Herald. *She wrote the best-selling book,* Women & Money.

Education about money

JOANNA McCREERY

Joanna McCreery, 20 years in the finance industry, is a certified financial planner and a director of Majella Wealth Advisers, a boutique financial advice firm.

Life has started tough for Megan Stammers, but thanks to her caring parents and community her financial future is off to a good start. Once she is 18 she will have enough money to allow her to make choices many her age would not be able to make – such as take a year off to travel, buy a car, further her education or invest to fund a future goal being just some of them.

With this opportunity goes responsibility for her parents to educate Megan well about the value of money. Too often a cash windfall is spent unproductively. If, by the time Megan receives the cash, she is responsible with money, there's a better chance she'll use it wisely. Preserving the real value of Megan's money means it needs to grow at least as much as inflation over time. If we assume inflation averages 3%pa over the next 16 years, $32,000 today needs to become $51,000 (after tax) in 16 years.

Some of the main options are a traditional bank account, a high-interest account or term deposit, and growth investments, such as shares. To access shares, they could invest some of the money in a portfolio of Australian shares directly through an online broking account or, more simply, one or a number of managed funds that invest into assets such as shares and property. Another alternative would be a capital-protected share investment.

With the bank accounts and term deposits Megan's cash is secure, but the expected return is relatively low. All interest is also taxable. An investment in growth assets such as shares is a lot more risky – the balance invested will fluctuate daily and could dramatically plunge in the short term – but the long-term return is expected to be higher. In addition, she would earn franking credits on the Australian shares, which will reduce tax. Tax on future capital gains will also be at half her tax rate.

The table shows what Megan's balance could be in 16 years, based on the returns shown. From July 1, 2011 child tax rates are effectively 45% for any taxable income over $416pa. Previously, the low-income tax rebate allowed children to earn a little more in their name before the penalty tax rates kicked in, but the government has recently decided not to allow children to claim this rebate. At these rates, a 5% return becomes only 2.6%pa after tax.

A lower tax option may be for one of Megan's parents to hold the investment in their name in trust for her. They would declare the income on their tax return and pay tax on it at their marginal tax rate. At a 30% marginal tax rate, a 5% return becomes only 3.5%pa after tax.

If they decide to invest a portion in shares, franking credits will reduce the tax payable. With companies such as our big banks paying fully franked dividends of 6-7%pa, a long-term holding in shares may be worth considering if they can accept the risk. At the 30% marginal tax rate, a 6% fully franked dividend stays at 6%pa after tax.

INVESTING $32,000

TYPE OF INVESTMENT	POTENTIAL LONG-TERM RETURN[1]	BALANCE AFTER 16 YRS[1]
Low risk: standard bank account	3%pa	$51,351
Low risk: high-interest bank account or term deposit	5%pa	$69,852
Medium risk: 50% low risk, 50% high risk	6%pa	$81,291
High risk: e.g. shares or managed share funds	7%pa[2]	$94,469

[1]Before tax. [2]Long-term expected return becomes less certain, but is expected to be higher than cash