How to set your kids up for life

By Kelly Baker · Jul 26th, 2017

It's hard not to feel depressed or anxious when you hear about cashed-up parents buying their eight-year-olds multi-million dollar homes for them to eventually move into, but don't let that prevent you from making plans of your own. Sure, you could jazz up a couple of refrigerator cartons in the hope the tiny houses trend will eventually branch out into abandoned white goods packaging, or you could speak with Laura Menschik, certified financial planner and director of WLM Financial, who insists there are plenty of other ways to provide your kids with a great financial start to life. The key to success? Working out what suits you, your family and your income best.

"Whether you've got $5,000 or $50,000 to invest, there are pluses and minuses for each type of investment you could make, from property and managed funds, to investment bonds and shares," she says.

"So it's important to take some time to think about how important flexibility is to you, what you can afford, and what your desired outcome is - for example, do you want your child to be able to access the money once they turn 18, or would you like to keep the investment rolling until they're in their mid to late 20s?"

Remember children under the age of 18 can only earn up to $416 per annum before they're taxed at a whopping rate of 66 per cent, so whichever way you decide, keep the investments in your name so that it's taxed at your own marginal tax rate. If you create a trust in your child's name so that the investment rolls over to them once they become an adult, the amount will then be taxed at their own marginal rate, which could work out to be a better option in the long-run.

"This year, for example, there's no tax on earnings of up to $18,200 and then it's only 19c for every dollar up until they're earning $37,000 so that could be a better bet for your child if you're a higher income earner."

In terms of investment options, you could consider:

Online savings accounts and term deposits

Once upon a time, high interest savers attracted parents like bees to honey, but their popularity as a safe and steady option has been in a long and sustained decline, says Menschik.

"With our low interest rates, this just isn't an effective strategy to accumulate wealth anymore, however parents often do enjoy the flexibility of having the money at hand."

Ditto with term deposits – cash investments held at a financial institution where your money is invested at an agreed rate of interest over a fixed amount of time.

Although, like online savers, term deposit returns won't be as high as with other options since you're relying on interest earnings alone to grow your capital rather than growing your capital balance, they do offer higher interest rates than traditional accounts, as well as protection from interest rate changes during the term of the deposit.

Managed funds

Otherwise known as a Managed Investment Scheme, these types of funds pool your investment with other investors in order to buy shares, property or other assets, and make periodic income distributions. Not as high-yield as buying ASX-listed shares, but often a safer choice, says Menschik.

"A number of managed funds have a lower investment range so they're an attractive option, but you must also put in a minimum amount each month such as a $100, so you need to look at your commitments carefully," she says.

"Aim to save up at least $5,000 for you initial investment if you can so that you have a lump sum that can make an impact as the years wear on, but note that some may require more than $10,000 or $20,000 depending of the manager of the investment product."

Considered a long-term investment, expect to commit for anywhere between 10 to 20 years to (hopefully) make a big difference to your child's life.

To save at tax time, consider investing within the name of the person who is taxed at the lower marginal tax rate.

Investment bonds

On a higher income? You may want to consider putting your cash in investment bonds – a long-term investment option offered by insurance companies and friendly societies that are similar to a managed fund. They not only include a handy little life assurance policy, but some much-appreciated tax breaks for those earning over $87,000 in particular.

"Think of it this way, someone who is earning $37,000 per annum is already being taxed at 32.5c in every dollar, while someone who is earning $87,000+ is taxed at 37c in every dollar, yet investment bonds are internally taxed at 30 per cent," she says.

"And if you keep it invested for longer than 10 years and then take out the money, it's tax-free."

Although investment bonds can be started with as little as $1,000, they do come with restrictions as to how much you can invest additionally each year.

"You can only add up to 125 per cent of what you put into the bond the year before, so – for example – if you put in $100 the year before, you'll only be able to put in $125 this year and so forth."

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Small girl, big future. Image: Getty.

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Your offset account

Nope, not a great wealth accumulation tool by any stretch of the imagination, but don't discount it without consideration, advises Menschik, who says that while you may not get a return as such, you will get other benefits.

"If you put the money you've been allocating for the kids into your mortgage each month, it won't earn much, but what it will do is reduce your mortgage quickly so that not only do you have more disposable income to play around with once the house is paid off, but you'll also have a fully paid house which will eventually pass on to them."

An additional benefit is that you can also easily withdraw funds from your offset should you need it quickly in an emergency.

Shares

Got a spare $5,000 to invest? Don't even bother with shares, warns Menschik, who says investing smaller amounts can't attain enough diversification to accrue wealth.

"Sure, you could put all your money in the one stock you're convinced is a sure bed, but if it falls, everything's gone so there's a lot of risk involved with taking that approach," she says.

Investing successfully in stocks usually takes an outlay of at least $20,000 (minimum) to distribute widely and then you'll have to keep an close eye on your investment – not exactly the kind of investment strategy who want to set and forget. If you are a serious investor with cash to burn however, you can work with a financial advisor to set you up with a beautiful share portfolio

No matter what you decide, remember to speak with a financial advisor first about which investment method would work best for your personal situation. You can find an advisor in your local area by checking out The Financial Planning Association of Australia.