Don't blow it

A windfall is not easily come by — and even harder to hang onto. EMILY CHANTIRI has some tips to make it last

You'd be hard pressed to find anyone who hasn't dreamt of winning a million dollars. The first things that come to mind are paying off the mortgage, buying the red sports car, money for the kids' education, taking the family on the holiday of a lifetime and quitting your job — the list is endless.

While you dream on, it's important to note that the statistics show people who come into large sums of money, say, through a lottery win, squander it within five years.

Naturally, the impulse is to rush out and spend the money, though a little preparation and some good financial advice might have made the fun last a whole lot longer.

On the other hand, self-made millionaires tend to remain frugal and prudent with their money, particularly if they started with nothing. It's often been said that making the first million is the hardest. And if you've done it the hard way, it's easy to remember what it was like to struggle financially.

The common mistake people make with a windfall is taking a short-term approach. Prudent management of a significant windfall can improve your lifestyle over your whole life, not just the next five years.

Financial adviser Lisa Faddy, of Majella Wealth Advisers, adds: "We've seen people who have inherited a large sum of money, or who have made a large gain on the sale of an investment property and proceeded to spend most of it. Only after realising much of it had gone did they seek advice! People often don't appreciate all that they can accomplish with the money.

"Acting too hastily, whether through excessive spending, inappropriate investments or 'short-termism', by which I mean looking at what they can do now, can see the money disappear all too quickly," says Faddy. "Seeking professional help can help clarify goals and available options.

"For example, do they want to buy a bigger house, reduce their debts or invest the windfall? Potentially, they can do all three.

"If a person is comfortable with the risks of gearing, they can establish an investment portfolio using the equity in their home," explains Faddy.

"Also, by reducing non-tax-deductible debt, such as the home loan, and investing part of the windfall, they can potentially improve their lifestyle over the long run."

HORSES FOR COURSES

Your age and stage of life will also determine the approach to the investment of a windfall. For older people, additional super contributions can be worthwhile. For younger people, paying off the home loan and using some of the remaining capital as equity to borrow for longer-term investing can effective.

"We have talked to people who have inherited a significant sum of money at a young age and have simply increased their spending patterns," says Faddy. "These people can benefit from a more disciplined approach to managing their funds.

"For instance, setting up a structure whereby they have a certain amount of funds to use from their windfall each month, almost like a salary, plus a strategy to use some of the capital to further grow their wealth.

"One problem with young investors is they often want to buy into businesses that interest them at that age. I knew someone at university who, in their early 20s, won the lottery and bought a nightclub. It did not turn out to be a profitable venture for him. Perhaps if he had worked for the money, he would have been more cautious about how he invested it."

HOW MUCH FUN CAN I HAVE?

Once you have adjusted to the prospect of never having to work again, there's nothing stopping you from enjoying part of your windfall. Be extravagant, take that unforgettable holiday, but just remember that this should be with only a sensible proportion of the winnings.

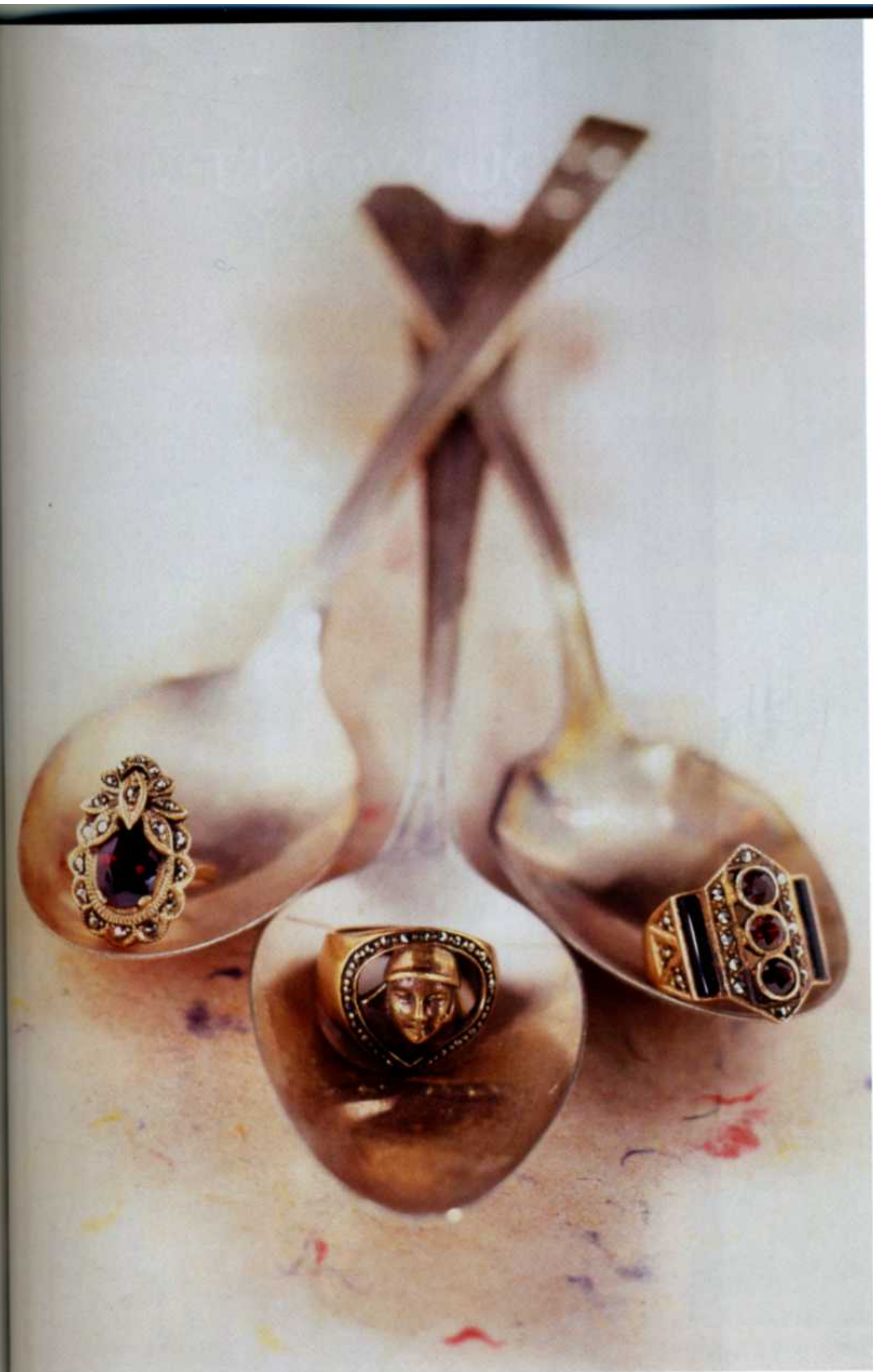
"If you are closer to retirement and already comfortably set for retirement, you can set aside a larger percentage, say 20 or 30 per cent. For a younger person, with ongoing future commitments, look to spend around 10 per cent now and plan to invest the balance," adds Faddy.

Maggie*, 47, and James*, 52, have been married for 17 years and have two children. Maggie received a large inheritance after the death of her parents. Eight years earlier, the couple had been through a similar experience after the death of James's parents. Although his parents' estate was much smaller, the couple put the inheritance straight into the mortgage. Apart from shortening the life of their mortgage, they felt no other significant financial changes. This all changed when Maggie received her inheritance.

"I had no idea how much money was coming through and I didn't know I would be the beneficiary — it was a complete surprise. The will was split three ways between my brother, myself and my children," says Maggie.

"The inheritance came through in both cash and shares. The first thing we did with the cash was to pay off the home loan. This decision was made in three days. We wiped the mortgage and this has made a significant difference to our lives in terms of cash flow. We no longer have mortgage payments.

"The immediate impact was I don't ever have to work again, even though I choose to work part-time. The children's money



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has been put into a trust for their education to cover all fees for private schools and university. This has freed us of long-term debt. Now we don't have any debt or any future debt."

Maggie's father, an accountant and keen investor, had accumulated a large share portfolio. The blue-chip shares returned high dividend yields annually.

Maggie decided to keep the share portfolio intact and the dividends she receives form part of her income. "I receive $35,000 a year in dividends from my share of the portfolio alone. My intention is to maintain an income from this portfolio until I die."

Maggie also came into conflict with other family members. They believed they were entitled to some of the estate. Sadly, this is a common complaint with windfalls.

"We did receive some underlying messages from other family members implying that they deserved some of the money," she says. "Although no case was put forward, my brother was very upset that my children got a third of the estate. He firmly believes he was entitled to 50 per cent. Probate has been granted and everything has now been settled. My brother is still very, very annoyed about this, and I understand, but this was how the will was set up."

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The couple plan to re-evaluate their portfolio every 12 months. The goal is to ensure the portfolio returns high dividends from their investments.

"Our preference is to keep all the money in high-dividend-yielding shares," Maggie says. "The kids wanted us to buy a sports car. We decided not to replace the car or do any renovations to the house, but we are going on a holiday for six weeks.

"I said to the travel agent, 'I want a really nice holiday. Don't send me to any cheap hotels.' She said, 'Do you want me to hire a Mercedes?' 'No,' I said. Even though we have the money, I don't think I could be that extravagant.

"I know the value of money and how hard it is to make a dollar, and this has informed all my decisions. I don't want to turn around and have to start working again at age 50."

* Names have been changed to protect privacy. These tips are considered opinions only and readers should seek personal finance advice. You can contact Emily Chantiri at emily.Chantiri@bigpond.com.au