



Macquarie Life

The benefits of insuring through super

While your clients are accumulating wealth, they should have adequate insurance cover to make sure they and their families are looked after in the event of the unexpected.

Deciding whether client insurance arrangements should be held inside or outside of super involves assessing the tax, benefit access and social security implications of each alternative. In many cases, super may be the best option, not just to finance that insurance cover but also to make sure the proceeds are paid in the most effective way if and when the time comes.

In this flyer we briefly outline some of the benefits of holding insurance within superannuation with regard to:

- financing premiums through super
- payment of the proceeds, and
- maximising its effectiveness.

Let's start with an example

Andrew is 45 years old and earns \$130,000 a year as a self-employed architect. His wife Gloria (also aged 45) is currently out of the workforce caring for their three young children. They have worked out that in the event of Andrew's death, they would need about \$550,000 of insurance cover to meet their current debts. For the purposes of this example, their income needs will be met through other investments. Both of them have substantial super balances within their superannuation accounts and Andrew contributes to his account, by way of tax deductible (concessional) contributions, as and when the cashflow from his business allows.

Let us compare the benefits of funding insurance cover through Andrew's super account versus a conventional stand alone policy outside superannuation (referred to as a non-super policy). We will assume the same premium in both cases.

The benefits of financing the premium through super

Cashflow benefits can bring peace of mind

When insurance is taken through a superannuation fund, the trustee can pay insurance premiums directly to the insurer from the individual's account balance within that fund. For Andrew, this removes the worry that, with his uneven business cashflow, there may be periods when he cannot make his premium payments.

Tax credits reduce contributions tax

Salary sacrifice contributions and personal contributions claimed as a tax deduction will attract income tax of 15% within the fund. However, to the extent the superannuation contributions are used to finance/pay the cost of the insurance premiums, part or all of the premiums may be tax deductible to the fund. Premiums for death cover are typically fully tax deductible within superannuation. Premiums for TPD and disability income cover within superannuation may be fully or partially deductible depending on certain conditions. Tax deductions can reduce the actual cost to the member. However, where cover is held through the insurance only division of the Macquarie Superannuation Plan, the tax effect of the deduction is not credited to a client's account where the contributions made to fund the premiums are not taxable (for example, where your client or their spouse has made non-concessional contributions).

Tax-effective outcomes

Premiums for personal insurance cover via a non-super policy are generally paid with after-tax dollars. On the other hand, premiums paid through a super fund can effectively be funded from concessional super contributions. In addition, tax concessions can apply to super benefits paid as a result of death, terminal illness or total and permanent disability. As a result, insuring via super can often be more tax-effective compared to insuring outside super. Andrew is currently self-employed, but that situation may change so we will look at the options available to him now and others that may apply in the future.

1. Tax savings for the self-employed

As in the case of Andrew, self-employed (or substantially self-employed) people below the age of 75 may be eligible to claim a tax deduction on personal contributions. These contributions are taxed at 15% by the fund up to an annual concessional contributions cap of \$25,000 in the 2011/12 financial year. However, for people aged 50 or more at any time in a financial year, their annual concessional contributions cap is \$50,000 until the financial year ending 30 June 2012.¹

Tax deductions for personal contributions may also be available for people whose sole source of income in a financial year is from investments rather than work.

2. Salary sacrifice can reduce the cost for employees

If Andrew or Gloria should become an employee at some later date, they may be able to arrange for their employer to make super contributions of an amount which includes the cost of the premiums for any life or disability cover, directly to their chosen superannuation account. Like personal deductible contributions, employer contributions are subject to 15% tax in the fund and are subject to the concessional contributions cap. Where these contributions are used to fund insurance premiums that are deductible to the fund, the overall effect is that insuring via super is often more tax effective compared to insuring outside super.

3. Government co-contributions boost super savings

If Andrew's or Gloria's work circumstances were to change, they might find themselves qualifying for a Government co-contribution which is available for certain employees and self-employed people who make personal non-concessional contributions to superannuation and whose total earnings for a particular year fall within limits set by the Government. If they qualify for this incentive, then it may be a very appealing way for them to make extra super contributions. Broadly, the Government co-contribution incentive works like this: if in a particular financial year an eligible person has total earnings² of less than \$31,920 (in the 2010/11 and 2011/12 financial years) and makes personal non-concessional super contributions, then for every \$1 of personal contributions made in that year up to \$1,000, the Government will contribute \$1. So, the Government co-contribution could be as much as \$1,000. If their earnings are between \$31,920 and \$61,920 (which are the thresholds for the 2010/11 and 2011/12 financial years) a lower maximum applies. No co-contribution is available if earnings are \$61,920 or more.

4. Paying for cover via spouse contributions may generate a rebate

While insurance needs tend to focus on the main breadwinner, there is clearly a case for providing cover for a non-working or low income spouse. If Gloria were to die, for example, Andrew would almost certainly need to employ someone to look after the house and help with the children. One tax-efficient way to insure Gloria as well could be to pay the premiums by way of a spouse contribution to her superannuation account. Depending on Gloria's income, fringe benefits and reportable employer super contributions, the contributor (in this case Andrew) may be able to claim a rebate of up to \$540. Alternatively, Gloria may contribute on her own behalf. In some circumstances it is possible for a non-working or low-income spouse to claim a tax deduction for their personal contributions. However, even where your clients do not claim a deduction or are not eligible for a Government co-contribution, there may still be circumstances where having premiums funded from personal non-concessional super contributions is a relatively tax-effective way to insure.

¹ In its response to the Henry Tax Review, the Government proposed to retain the higher concessional contributions cap of \$50,000 for individuals aged 50 and over with total super balances below \$500,000 from 1 July 2012. The Government is consulting with the industry on the operation of the \$500,000 threshold.

² 'Earnings' means assessable income plus reportable fringe benefits total plus reportable employer superannuation contributions.

Maximising the effectiveness of insurance cover

Macquarie Life's product suite provides a range of features that allow you to structure cover for your clients in the most effective way. Cover can be structured seamlessly inside and out of super so that your client can have comprehensive cover without losing any of the benefits of insuring through superannuation.

Variable levels of cover

Variable levels of cover are available, so that the levels of cover can be tailored to each client's specific circumstances. Under all products, higher levels of Life cover may be taken for debt and estate planning where dependants are involved, while under FutureWise, higher levels of TPD cover may be taken for those without dependants or those who want cover to provide for a greater level of expenses that may be incurred with TPD.

Flexible Linking

Flexible Linking is a way of structuring cover so that insurance for the same insured person can be held under separate policies with different policy owners but still be treated as linked insurance. For example, insurance may be held under one policy that is owned by the trustee of a superannuation fund and be connected to a policy owned by the insured person outside of superannuation such as through superannuation optimiser (see below).

For example, under FutureWise this means that Life and TPD can be taken within superannuation and the tax effectiveness of such structuring preserved, while at the same time allowing your clients to access important Trauma outside of superannuation.

Self managed superannuation funds

Where a trustee of self managed superannuation fund is considering taking out insurance cover through their fund, it is important to understand that the trustee is responsible for considering:

- the appropriateness of providing each type of insurance cover and the implications for the complying status of the fund,
- the tax consequences of holding the cover, and
- super laws that operate to limit the release of benefits.

Superannuation optimiser

FutureWise

Under this feature the *own occupation* definition of TPD can be applied for with the part of the TPD Insurance that meets the Superannuation Industry Supervision Act (SIS) definition of permanent incapacity held within superannuation and the remainder of the cover held outside of superannuation.

Typically the premium paid in respect of the TPD cover held inside superannuation is fully deductible.

Sumo

Superannuation optimiser is available to trustees of self managed superannuation funds. Where any TPD Insurance is held inside superannuation, *superannuation optimiser* applies only to the cover provided under the Standard TPD tier and not

to cover provided under the Sumo TPD tier, which is held wholly inside superannuation.

Where the TPD sum insured falls within the Standard TPD tier, typically the premium paid in respect of the TPD cover held inside superannuation is fully deductible.

Where some of the TPD Insurance is provided under the Sumo TPD tier, the premium paid in respect of the TPD cover held inside superannuation will, from 1 July 2011, be deductible to the extent that it relates to the fund's liability to pay a "disability superannuation benefit" as defined in tax law and actuarial certification may be required.

Active

While some parts of this cover cannot be held within superannuation, a client may choose to structure the insurance under a Superannuation Optimiser arrangement which involves:

- a policy held by a super fund which provides cover for insured events that align with conditions of release in super law (ie death, terminal illness and permanent incapacity), and
- a separate, linked non-super policy providing the remainder of the cover.

The premium paid for the policy held within superannuation is generally tax deductible to the super fund.

Extra Benefits cover

The Extra Benefits policy is available in conjunction with Disability Income Insurance and Income Cover under FutureWise. If a FutureWise Disability Income Insurance policy or Active Income Cover policy is held within superannuation, the Extra Benefits policy is provided under a separate non-super policy to provide the following benefits: Specific Injury benefit, Trauma benefit, Bed Confinement benefit, Home Care benefit, Rehabilitation Expenses, Accommodation benefit, Future Increases and Cover Extension. This allows Disability Income Insurance and Income Cover to be held and funded through superannuation, without forgoing the comprehensive cover provided by the Extra Benefits policy, which pays amounts that may not be able to be released from a super fund under super law.

TPD Commutation option

This option allows the client to elect to receive the FutureWise Disability Income Insurance benefits as a lump sum in place of ongoing income, if the insured person meets the *any occupation* definition of *total and permanent disablement* and meets the definition of permanent incapacity as defined in superannuation legislation.

Taking cover through a super fund can often mean that premiums are paid from pre-tax, or concessional dollars.

The end result

The table below sets out how much pre-tax income Andrew needs to earn (based on a marginal tax rate of 38.5% applicable to his income of \$130,000 pa) to fund an annual insurance premium of \$645.15 via a policy providing death cover held within superannuation and via a non-super death cover policy.

Andrew as a self-employed contributor	Fund via super (personal concessional contributions)	Fund via non-super policy (after-tax dollars)
Insurance premium ³ (A)	\$645.15	\$645.15
Tax payable (B)	\$96.77 (Contributions tax = \$645.15 x 15%)	\$403.87 (Income tax = \$645.15 / (1 - 38.5%) x 38.5%)
Credit for the fund deduction for the premium ⁴ (C)	\$96.77 (Deduction = \$645.15 x 15%)	Not available
Gross cost to individual (A+B-C)	\$645.15	\$1,049.02
Amount saved by insuring through super	\$403.87	

The table below shows the cost of insuring via a non-super policy for different income tax rates and shows the gross amount that could be saved by insuring the same policy through super using salary sacrifice contributions.

Andrew as an employee	Fund via super (employer concessional contributions)	Fund via non-super policy (after-tax dollars)	Fund via non-super policy (after-tax dollars)	Fund via non-super policy (after-tax dollars)
Effective rate of tax	0% (15% contributions tax offset by credit for the fund deduction for the premium)	46.5%	38.5%	31.5%
Gross cost to individual	\$645.15 ³	\$1,205.89	\$1,049.02	\$941.82
Amount that could be saved by insuring through super		\$560.74	\$403.87	\$296.67

The table below shows how much Gloria would have remaining from her salary to invest for retirement after funding the insurance premium for \$550,000 of life cover through a superannuation policy when compared to a non-super policy. In this example, Gloria has returned to work part-time, earning an assessable income of \$40,000 pa (and she does not have any fringe benefits or reportable employer super contributions).

	Fund via super (personal non-concessional contribution)	Fund via non-super policy
Pre-tax salary (A)	\$716.61	\$716.61
Tax payable (B)	\$225.73 (Income tax = \$716.61 x 31.5%)	\$225.73 (Income tax = \$716.61 x 31.5%)
After-tax contribution to super (C)	\$490.88 (= A-B)	
Plus credit for the fund deduction for the premium ³ (D)	\$73.63	
Premium ² (E)	\$490.88	\$490.88
Plus Government co-contribution (F)	\$490.88	
Funds invested for retirement	\$564.51 (= C+D-E+F)	N/A

³ Based on \$550,000 FutureWise Life Insurance annual premium for an insured person aged 46 next birthday, non-smoker in NSW (male: \$1,1730 and female: \$0.8925 per \$1,000 sum insured).

⁴ Assumes that no deduction for the premium for the non-super policy applies and that the super fund can claim a full deduction for the premium. A tax credit is not available under FutureWise Super where premiums are funded with non-concessional contributions.

Please note: – all income tax rates are those applicable in 2010/11
– we assume that the insurance benefit will not be subject to income tax (ie it will be paid as a lump sum to a dependant for tax purposes).



Payment of the proceeds

While funding insurance through superannuation has great advantages in terms of cashflow convenience and cost savings, clients also need to consider the tax treatment of the insurance proceeds when a death or disability occurs.

Death

For Andrew and Gloria the situation is uncomplicated. Andrew is a member of a super fund which allows him to make certain types of death benefit nominations. He has made a non-lapsing death benefit nomination specifying that Gloria is to receive the benefit. If he dies she will receive a total payment of \$900,000 comprising his account balance of \$350,000 plus the insurance proceeds of \$550,000. Gloria is a dependant under superannuation and tax legislation, so she can receive the entire payment as a lump sum free of tax just as she would if it had been set up under a conventional (non-super) insurance policy. Alternatively, she may be able to receive the death benefit from the fund in the form of an account-based pension which would either attract a 15% tax offset or be free of tax (depending on age).

Conversely, if the lump sum was instead paid to someone who was not a dependant, it may include an “untaxed element” which is taxed at 30% plus the Medicare levy, while the “taxed element” is taxed at 15% plus the Medicare levy.

Child allocated pensions

In Andrew’s case, as he is a member of a fund that offers non-lapsing nominations and child pensions, Andrew can choose to have part or all of his benefit paid as account-based pensions to each of his three minor children. Not only are child pensions a tax-effective estate planning tool, they are a simple but effective way of managing and controlling the distribution of superannuation savings amongst beneficiaries.

Total and Permanent Disability

Total and Permanent Disability (TPD) benefits have different tax treatment from death benefits paid through super. The tax treatment depends on age, and tax concessions can apply where certain conditions are met. Additionally, not only can the policy definitions for TPD affect the extent to which the super fund can claim a deduction for the premium but also whether or not the proceeds can be paid from the super fund under preservation rules. Careful consideration needs to be given to the definitions available when assessing the merits of insuring for TPD inside or outside of super. As we noted earlier, Macquarie Life offers a TPD definition that structures some cover inside superannuation and some outside of super, which offers certainty in terms of the deductibility of the premium paid by the fund and the ability for benefits to be paid out of the fund.

Disability Income and Income Cover

Most people think that it’s only the major events such as death or TPD that are likely to have significant financial implications for them or their family. But how would your clients cope if they lost their ability to earn an income even if for only a short period of time? FutureWise and Active also allow members of Macquarie Wrap superannuation account (or badged version) to obtain Disability Income Insurance or Income Cover, respectively, through their superannuation account. This means they will receive replacement income, paid in the form of a taxable monthly income stream, if they are unable to work for an extended period of time due to sickness or injury and meet the benefit payment criteria set down in super law. Alternatively, as we noted earlier, the TPD commutation option available through FutureWise gives clients the choice to take their disability income benefits as a lump sum if they suffer TPD.

Macquarie Life's comprehensive product range

Product	Ownership
Macquarie FutureWise is our competitively-priced retail offering, delivering a comprehensive range of products and award-winning value.	Cover can be owned in and outside of superannuation: <ul style="list-style-type: none">■ individual or joint■ company■ SMSF■ insurance-only division of the Macquarie Superannuation Plan, or■ linked to a Macquarie Wrap superannuation account (or badged version).
Macquarie Life Active is a genuine all-in-one solution covering all major health events, death and terminal illness. It provides broad coverage for a range of conditions and unlike many other insurance policies, allows multiple claims over the life of the policy.	
Macquarie Sumo is a unique product for ultra high net worth clients – offering sums insured previously unavailable in the Australian market.	Cover can be owned in and outside of superannuation: <ul style="list-style-type: none">■ individual or joint■ company■ SMSF.

Useful resources

For more details on insuring through super please refer to the “Ins and outs of insuring through super” booklet, available on our website macquarielife.com.au/advisers.

Terms in *italics* have a special meaning and are explained in the glossary at the end of the FutureWise, Active and Sumo product disclosure statements.

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