Did you know?

Alex Koodrin
National Technical Manager

5 July 2013

Group insurance outside super

Group insurance arrangements are implemented to provide life insurance cover for groups of people, usually groups of employees. They are also provided by public offer and employer-sponsored superannuation funds. However, this article will focus on the tax and other issues related to group insurance arrangements owned by employers, outside of superannuation.

The most common insurances offered through group arrangements are term life, total and permanent disablement (TPD) and income protection (salary continuance). The main differences between group and individual insurances is that individual policies are fully underwritten, whereas group policies generally have automatic acceptance (i.e. no or limited underwriting assessment) up to certain levels of cover, and the policies are usually provided at cheaper, group rates. At the same time, the products offered via group arrangements are generally not as fully featured as retail offerings.

Most group policies are now under the superannuation umbrella, where the tax and release treatment of benefits is well known. Many of these policies were transitioned from non-super schemes following the more onerous tax treatment of the latter after the Simple Super changes in 2007. For various reasons, however, there are still many non-super employer-sponsored group insurance arrangements in place. They generally fall into two categories, as follows:

1. Employer takes out and pays for group policies on its employees for its own benefit, to fund its obligations – as an employer – to pay agreed termination amounts arising from death, TPD and so on. These premiums are tax deductible to the employer and there is no Fringe Benefits Tax (FBT) payable[1]. The payments to the end recipients are Employment Termination Payments (ETPs) and taxable in those recipients' hands as follows:

   Death benefit ETPs:

   - May be split into taxable and (if applicable) tax-free components
   - Taxable component payments to tax dependants[2] (directly or via the estate) are not subject to tax up to $180,000[3], with the remainder taxed at the highest marginal tax rate (plus Medicare levy)
   - Taxable component payments to tax non-dependants are taxed at 30 per cent up to $180,000 (plus Medicare levy), with the remainder taxed at the highest marginal tax rate (plus Medicare levy).

   TPD benefits (Life benefit ETPs):

   - May be split into taxable and (if applicable) tax-free components
   - Benefit payment may include an increased tax-free component
   - Taxable component up to $180,000 current ETP cap is taxed 15 per cent if employee is over their preservation age on the last day of the year of income and 30 per cent if below preservation age plus Medicare levy.
   - Taxable component over $180,000 current ETP cap is taxed at highest marginal tax rate plus Medicare levy.

---

[1] FBT is generally not payable on insurance premiums paid by the employer provided the employee is not a party to the insurance contract.
[2] For tax purposes, a dependant is defined as a spouse, including de facto, former spouse, child under the age of 18, financial dependant or person in an interdependency relationship.
[3] ETP cap amount is $180,000 for 2013-14. Indexed on 1 July each year, indexed to AWOTE and rounded up to nearest multiple of $5,000.

Income protection (salary continuance) benefits:

- FBT is not payable
- Benefits are assessed as ordinary income of the employee

2. Group policy is held by the employer (could also be another entity such as a professional association), but only legally. The beneficial ownership rests with the insured and the legal owner has no beneficial entitlement to any insurance payment. In this arrangement, the premiums may be paid by the employer (in which case there is an FBT liability), or by the insured. In any case, a claim payment is paid beneficially to the insured and is not an ETP. As this is for personal risk protection, there is no tax payable on the benefit*.

* Note that any income protection insurance benefits would be assessable in the hands of the insured.

Summary

Employer-sponsored group insurance arrangements are available both inside and outside superannuation

The tax treatment of a benefit ETP to tax dependants may be more onerous as compared to benefit payments under a group policy inside super.

CommInsure