Did you know?

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Life insurance policies in SMSFs – trustee implications

There is a tremendous shift in the focus of individuals to take control of their own retirement funding. Currently in Australia, there are more than 509,000 Self-Managed Superannuation Funds (SMSFs), with more than 963,000 members[1]. Over the past 12 months there has been an increase of 33,000 new funds and 64,000 new members. [2] Less than 13% of existing SMSFs have any life insurance.[3]

Trustees of a self-managed superannuation fund (SMSF) must also have an investment strategy that addresses insurance for each member of the fund. This does not make insurance mandatory, but it forces the trustee to review the insurance requirements on a regular basis (i.e. – annually) for each member (section 4.09 (2(e)) Superannuation Industry (Supervision) Regulations 1994). This requirement was enacted in 7 August 2012.

The Government also confirmed when implementing these changes that trustees should be self-reliant when determining the type and level of insurances required and that to meet this requirement the trustee should consider the personal circumstances of fund members as well as other legislative requirements, such as the sole purpose test.

ASIC Consultation Paper 216 has proposed disclosure requirements for SMSFs regarding life, TPD, and income protection insurance.[4] Therefore, when implementing or reviewing the fund's investment strategy, a trustee will need to consider a range of issues when determining each member's insurance needs and whether they should hold a death or disability policy for them. These issues include:

- the member's age, health, assets, liabilities, income level and whether they have any dependants
- whether the member has any existing insurance cover held inside the SMSF, in another super fund, or outside super and the level and type of those insurances
- whether the member, and or their dependants, would be able to maintain their current quality of life in the event of the member's death or in the event that the member was unable to work due to their temporary or permanent invalidity.

The trustees should document their decision in the fund's investment strategy or alternatively in the minutes of a trustees meeting.

It is important to note that this new rule only requires trustees to consider the need to hold insurances for member. It does not require a trustee of an SMSF to provide a minimum or default level of insurance for each member.

As the trustees of the SMSF are also the members of the SMSF, it should be relatively straightforward for each trustees to ensure that appropriate insurance strategies are addressed for the respective members.

When conducting the annual review of the insurance strategy of the SMSF, trustees will now need to consider what types of insurance policies (and their definitions) can be held by the SMSF.

New rules from 1 July 2014

On 1 March 2013, the Superannuation Legislation Amendment Regulation 2013 (No. 1) received Royal Assent. This legislation will have a significant impact on insurance in superannuation from 1 July 2014.

[1] ATO – Self managed super fund statistical report – June 2013
[2] ATO – Self managed super fund statistical report – June 2013
[3] Super System Review – 30 June 2010.
[4] Australian Securities and Investment Commission – Consultation Paper 216 – Advice on self-managed superannuation funds: specific disclosure requirements and SMSF costs (September 2013)

A regulated superannuation fund (APRA regulated or ATO regulated) may only provide an insured benefit to a member who joins from 1 July 2014 that satisfies a condition of release under Schedule 1 of the Superannuation Industry Supervision Regulations:

- Death (Item 102)
- Terminal Illness (item 102A)
- Permanent Incapacity (Item 103)
- Temporary Incapacity (Item 109)

Trauma insurance
Trauma insurance will be prohibited for any new member of a superannuation fund from 1 July 2014.

Grandfathering
Any existing insurance arrangements in superannuation for existing members that was in place prior to 1 July 2014 will be "grandfathered" and are permitted. Members of superannuation funds will need to be careful to ensure that they do not lapse their policies within superannuation, as the member runs the risk of any reinstated policy losing the grandfathered benefits.

Implications of new rules

In the past, trustees of superannuation funds simply purchased "ordinary" insurance policies. These policies were owned by the SMSF trustee, and any insurance benefits were paid to the SMSF. If the insurance benefits did not meet a condition of release, they were merely retained in the fund and credited to the respective member's account.

From 1 July 2014, SMSF trustees must ensure that any new policy that is purchased on behalf of a member meets a SIS condition of release in all circumstances for all benefits, features and options under that policy.

Under a typical "ordinary" policy, various ancillary benefits, plus benefits, or built-in benefits may not align with a SIS Act or SIS Regulation condition of release. These may include, but are not limited to: "own occupation" TPD; trauma benefits; guaranteed agreed value income protection; specified injury income protection benefits; critical illness income protection benefits; certain "loss of limbs or sight" TPD benefits; and financial planning benefits. While these benefits are terrific outside of superannuation, they may breach the new SIS Act or SIS Regulations for any new policy issued from 1 July 2014.

CommInsure's response
On 11 May 2014, CommInsure launched an "SMSF Plan" to ensure that SMSF trustees may have an insurance policy within their fund that aligns with the SIS Act and SIS Regulations. This means that in every circumstance, when CommInsure pays any benefit to the SMSF trustee from the "SMSF Plan", the SMSF trustee can be certain that the benefits meet an automatic condition of release and will not be retained within the fund (unless they want them to).

CommInsure has done the hard work on behalf of the SMSF trustees, so the SMSF trustees can have peace of mind that their insurance policies align with the SIS Act and SIS Regulations.

Summary
Significant changes have just occurred regarding any new insurance policy issued in superannuation from 1 July 2014. Income protection and TPD are most affected with definitions becoming more restrictive in order to align with SIS conditions of release.

From 11 May 2014, CommInsure has amended its products in order to comply with the new requirements.