MACQUARIE LIFE

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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.

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 explain 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 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. 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. This can reduce the actual cost to the member. In the case of Macquarie Super Protector and FutureWise Super, the credit for the tax deductible expense of the insurance offsets the effect of the 15% income tax.

Tax-effective outcomes

Premiums for personal insurance cover via an ordinary 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 concessionally taxed 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 $50,000 for the 2008/2009 financial year and $55,000 for the 2009/2010 financial year. However, for people aged 50 or older at any time in a financial year, their concessional contributions cap is $100,000 each year until the financial year ending 30 June 2012.

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 the 15% tax in the fund up 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 typically 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. In some cases, such as the example on the next page where Gloria returns to work, the co-contribution may even amount to more than the cost of their insurance cover. Broadly, the Government co-contribution incentive works like this: if in a particular financial year an eligible person has total earnings[1] of less than $30,342 (in 2008/2009) and makes personal super contributions, then for every $1 of personal contributions made in that year up to $1000, the Government will contribute $1.50. So, the Government co-contribution could be as much as $1500. If their earnings are between $30,342 and $60,342 (which are the thresholds for 2008/2009) a lower maximum applies. No co-contribution is available if earnings are $60,342 or more. The co-contribution thresholds are indexed annually in line with wages.

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 and fringe benefits, 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 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] 'Earnings' means assessable income plus reportable fringe benefits total. From 1 July 2009, it will also include salary sacrifice and certain other employer contributions.

Maximising the effectiveness of insurance cover

Macquarie Life's FutureWise and Super Protector products provide 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 Life and TPD Insurance are available, so that the levels of cover can be tailored to each client's specific circumstances. Higher levels of Life cover may be taken for debt and estate planning where dependants are involved, while 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.

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.

Superannuation optimiser definition of TPD

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.

The policy terms for the *superannuation optimiser* definition of TPD have been designed to meet tax law requirements enabling the Trustee to claim a full deduction for the premium payable by the fund, being the 'superannuation component'. The premium relating to the 'non-superannuation component' is not payable under a superannuation policy and therefore is not a deductible expense to the Trustee.

Extra Benefits cover

The Extra Benefits policy is available in conjunction with Disability Income Insurance under Super Protector. 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, Accommodation benefit, Future Increases and Cover Extension. This allows the Disability Income Insurance to be held and funded through superannuation, without forgoing the comprehensive cover provided by the Extra Benefits policy, which typically cannot be held within superannuation.

TPD Commutation option

This option allows the client to elect to receive the 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.

Macquarie Life's comprehensive product range

OUTSIDE SUPER	INSIDE SUPER
Macquarie FutureWise is our competitively-priced retail offering, delivering a comprehensive range of products and award-winning value.	**Macquarie FutureWise** is available to members of self managed super funds who would like to take advantage of the comprehensive cover provided through the retail product.
Macquarie Sumo is a unique product for ultra high net worth clients – offering sums insured previously unavailable in the Australian market.	**Macquarie FutureWise Super** delivers comprehensive cover and value for clients who are eligible to contribute to super.
	Macquarie Super Protector is available via the Macquarie Wrap platform to members of the Macquarie Superannuation Plan and self managed super funds. It provides an easy and comprehensive insurance solution.

Taking cover through a super fund can often mean that premiums are paid from pre-tax, or concessionally taxed, 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 41.5% applicable to his income of $130,000 p.a.) to fund an annual insurance premium of $720.50 via a policy held within superannuation and via an ordinary policy.

Andrew as a self-employed contributor	Fund via superannuation (personal concessional contributions)	Fund via ordinary policy (after-tax dollars)
Insurance premium[2] (A)	$720.50	$720.50
Tax payable (B)	$108.08 (Contributions tax = $720.50 x 15%)	$511.12 (Income tax = $720.50 / (1 - 41.5%)) x 41.5%
Credit for the fund deduction for the premium[3] (C)	$108.08 (Deduction = $720.50 x 15%)	Not available
Gross cost to individual (A+B-C)	$720.50	$1,231.62
Amount saved by insuring through super	$511.12	

The table below shows the cost of insuring via an ordinary 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 superannuation (employer concesssional contributions)	Fund via ordinary policy (after-tax dollars)	Fund via ordinary policy (after-tax dollars)	Fund via ordinary policy (after-tax dollars)
Effective rate of tax	0% (15% contributions tax offset by credit for the fund deduction for the premium)	46.5%	41.5%	31.5%
Gross cost to individual	$720.50[3]	$1,346.73	$1,231.62	$1,051.82
Amount that could be saved by insuring through super		$626.23	$511.12	$331.32

The table below shows how much Gloria would have remaining from her salary to invest for retirement after funding the insurance premium through a superannuation policy when compared to an ordinary policy. In this example, Gloria has returned to work part-time, earning an assessable income and reportable fringe benefits of $35,000.

	Fund via superannuation (personal non-concessional contribution)	Fund via ordinary policy
Pre-tax salary (A)	$754.74	$754.74
Tax payable (B)	$237.74 (Income tax = $754.75 x 31.5%)	$237.74 (Income tax = $754.75 x 31.5%)
After-tax contribution to super (C)	$517.00 (= A-B)	
Plus credit for the fund deduction for the premium[3] (D)	$77.55	
Premium[2] (E)	$517.00	$517.00
Plus Government co-contribution (F)	$775.50	
Funds invested for retirement	$853.05 (= C+D-E+F)	0.00 (= A-B-E)

[2] Based on $550,000 Super Protector Life Insurance annual premium for an insured person aged 46 next birthday, non-smoker (male: $1.31 and female: $0.94 per $1,000 sum insured).

[3] Assumes that no deduction for the premium for the ordinary 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 2008–09;
– We assume that the insurance benefit will not be subject to income tax (i.e. 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. Conversely, if the amount 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. 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. Refer to the '*Superannuation optimiser*[4] definition of TPD' section on the next page.

TPD expenses, because of their extended nature, are often far greater than the amount clients feel comfortable leaving to their dependants if they die. And for clients without dependants, insuring themselves for TPD may be far more important than Life cover. Variable levels of Life and TPD cover can be invaluable from a planning perspective.

Disability Income

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? Macquarie Super Protector also allows members of an *eligible superannuation plan* to obtain Disability Income Insurance 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. Alternatively, an option is available that gives clients the choice to take their disability income benefits as a lump sum if they suffer TPD. Refer to the 'TPD Commutation option' section on the next page.

[4] Terms in *italics* have a special meaning and are explained in the glossary at the end of the FutureWise and Super Protector product disclosure statements.

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