



# SMSF

## Insurance in Super - to have or not to have

Is it better to hold insurance policies inside your superannuation fund, or in your personal name? The answer is ... it depends on your circumstances. Holding your insurance cover within your super fund is a tax effective way to pay insurance premiums, and certainly helps your cashflow if you would prefer not to pay the premiums from your personal funds. However, it may also be harder to gain access to certain insurance proceeds from super in the event of an accident or illness if you do not meet an appropriate 'condition of release'.

### Things to Consider

**Table 1: Pros and Cons of holding Insurance Policies inside Superannuation**

Pros	Cons
Eligible individual may be able to make tax deductible contributions to superannuation which can help fund insurance premiums	Beneficiary has to be SIS dependant.
Super Funds can claim tax deductions for insurance premiums	Higher tax rate if benefits are paid to nondependent's on death of the member
Individuals may be eligible for a government co-contribution payment which can help fund insurance premiums	Tax may be payable on TPD benefits
Proceeds are tax free when death benefits are paid to dependant/s	Premiums used to fund insurance will reduce members retirement savings
Salary sacrifice can fund insurance premiums	
Premiums may be cheaper if accessed via a super fund offering group rates	
Group plans may offer automatic acceptance to certain levels of cover (no underwriting requirements for the client)	

Source: RBS Morgans

### **Insurance Premiums - Deductible or Not?**

Life and Total & Permanent Disability (TPD) insurance policies owned by an individual are not tax deductible to the individual. Premiums on income protection insurance, however, are tax deductible to the individual.

Insurance premiums on Life and TPD policies owned by a super fund are generally tax deductible to the fund.

However, when a death benefit payment is subsequently made on death of a member an untaxed element will arise as a result. If payment of death benefits from this untaxed element is made to a non-dependant adult child, the payment will be taxed at the rate of 31.5%, which is a higher rate than the standard 16.5% tax rate payable on death benefits from a taxed element.

If a death benefit payment is made to a tax dependant then it will be 100% tax free. This is regardless of whether the death benefit payment includes the untaxed element or not.

If a super fund chooses *not* to claim a deduction for insurance premiums during the life of the member, when a death benefit payment is made the fund can claim the total death benefit payment as a deduction against the fund at that time. This process is only of benefit to the super fund; however, if there is the intention or ability to pass the fund through to the next generation, particularly for self managed super funds.

### **Deductibility of TPD Insurance Premiums from 1 July 2011**

To access TPD insurance benefits within superannuation the member must meet two sets of criteria:

- Firstly, they must meet the insurer's definition of TPD. Money is then paid to the member's benefit account.
- Secondly, before the super fund can release the benefits the member must meet the permanent incapacity condition of release.

That is, where the Trustee is reasonably satisfied that the member is unlikely, because of ill-health, ever again to engage in gainful employment for which the member is reasonably qualified by education, training or experience – or the 'any occupation' definition of TPD. The 'any occupation' definition is the acceptable definition contained in the superannuation rules (SIS Act) and premiums paid by the super fund under this definition will be tax deductible.

**From 1 July 2011 a TPD insurance policy held within superannuation under 'own occupation' definition, which is a much narrower definition of incapacity, may not be deductible to the super fund.**

Why? In the past premiums paid on TPD insurance policies held within super have been 100% deductible regardless of whether it is 'own' or 'any' occupation definition. However, in October 2009 the Federal Government announced that TPD insurance premiums will only be deductible to the extent the policies have the necessary connection to the liabilities of the super fund to provide 'any occupation' benefits. It was never the intention of existing tax legislation to allow super funds full deductibility of premiums for benefits that exceeded what could be released, or could not be released, in accordance with the SIS conditions of release.

A subsequent transitional period was announced so that super funds could prepare themselves and make any necessary changes to their policies. **This transitional period ends on 30 June 2011.**



### **'Own Occupation' Definition**

Under the 'own occupation' definition, the insurer agrees to pay an amount to the policy owner when the insured individual is unable to perform the duties of their own occupation. This definition is a more specific definition for incapacity compared to the 'any occupation' definition. 'Own occupation' insurance is popular with specialists in the medical field, for example, as it covers their inability to perform their own specialist duties, even if they may be able to continue practising in the more general medical space. The problem is the individual may not automatically access benefits paid unless the broader 'any occupation' definition can be met.

### **'Any Occupation' Definition**

The 'any occupation' definition is where the insurer agrees to pay an amount to the policy owner when, because of a physical or mental ill health, the insured individual is unlikely to engage in gainful employment for which they are reasonably qualified by education, training or experience.

We recommend super fund members review any insurance policies held within their super fund as soon as possible, and discuss with their adviser to determine whether a more appropriate and cost-effective strategy is required after 1 July.

### **Payment of TPD Insurance Benefits**

Payment of TPD insurance benefits to a super fund member are not tax free. Only the tax free portion of a member's account will be tax free. Tax will still be payable on the taxable component.

There may be further taxation relief to the member if they meet the criteria of a Disability Superannuation Benefit:

- the benefit must be paid because a person suffers from ill-health (physical or mental)
- two legally qualified medical practitioners must certify that due to ill-health, the person is unlikely to ever return to gainful employment for which they are reasonably qualified due to education, experience or training.

### **Transferring Existing policies into Super**

An individual cannot transfer an existing life insurance policy to their superannuation fund as it would breach the acquisition of assets rule. But in certain circumstances the policy can be cancelled and reissued by the insurance company (and generally without the client having to go through the underwriting process again).

Note: don't assume that a company will act on a request to cancel and reissue an individual's policy; check with the respective new business or underwriting team first to make sure it can be done and what the process is.

With thanks to RBS Morgans for the information above on insurance in superannuation.

***Please note that the information above is of a general nature and is not intended to be comprehensive nor does it constitute specific advice. Always seek independent financial advice before making decisions.***

**Always remember that we are available to assist our clients with any questions regarding self managed superannuation funds. Please feel free to email your questions to our office or to give us a quick call if you are unsure of any actions surrounding your fund. Please also inform us of any topics you would particularly like to see in future newsletters!**

