Brian Jones, Managing Director

MAKE A DIFFERENCE insurance

Insurance Within Self Managed Super Funds

There are more than half a million Self Managed Super Funds (SMSFs) in Australia with over 900,000 members and an average value of just under $1m. With just 13% of trustees having insurance within their SMSF, the importance of Advisers assisting fund Trustees with the new legislation is crucial.

As part of the Stronger Super Reforms introduced by the Government in August 2012 Trustees of SMSFs are now required to consider insurance for their members as part of the fund's Investment Strategy and keep a documented record of the discussion of this issue.

Fund Auditors have a legal duty to report any breach of this requirement to the Australian Taxation Office.

These are four types of insurance that you can purchase through your SMSF:

1. **Life Insurance** pays a lump sum benefit to your family or nominated beneficiary event of your death.

   This lump sum amount can help with major financial expenses such as paying off a home loan, children's education and funeral expenses.

2. **Total and Permanent Disablement Insurance** pays you a lump sum or income stream to the insured in the event of disability due to injury or accident. The payment can be used to cover extra medical and rehabilitation costs associated with the disability.

3. **Income Protection Insurance** pays you up to 75% of your gross monthly income if you are unable to work because of an illness or injury.

4. **Trauma Insurance.** Although Trauma Insurance (cancer, heart attack, stroke etc) can be owned by a SMSF, rules are changing so ensure you talk with your Adviser.

Considerations

Insurance within SMSFs is not a one size fits all approach. The various issues that a trustee and their adviser must consider include:

1. Tax deductibility of the contributions used to pay for premiums inside superannuation versus the tax deductibility of the premiums outside superannuation.

   For members of a SMSF, there are generous tax incentives available when you take out personal Life Insurance through your fund. The SMSF funds used to pay the insurance premiums are taxed at the 15% super contribution rate, whereas if were you to purchase Life Insurance, TPD Insurance or Income Protection policies personally, you would be using after tax dollars.

2. Tax assessment of the insurance benefits when paid from superannuation versus the assessability of the same benefits if the policy was held outside of super.

3. Affordability – it is better to have some insurance cover than none at all. Some individuals may struggle financially, and thus may only be able to afford Life Insurance premiums via their superannuation fund.

4. Limited Recourse Borrowing Arrangements (LRBA) – if an SMSF has a LRBA, then the trustees may need to consider how to best extinguish this debt upon the death or permanent incapacity of a member.

5. Existing insurance arrangements via other superannuation providers or held in the individual member's name.

6. Family situation and dependents – consider how much insurance in enough to ensure the family is not left in financial stress in the event of the death of the member of the SMSF. Dependents – the number of dependents and the age of those dependents may impact upon whether the insurance should be held inside or outside superannuation (in particular, adult age children).

7. Existing debts – ensure that the member can pay off any debts in the event of Total or Permanent Disability (TPD) or death.

8. Maintaining the existing standard of living – in the event a member is sick or injured, having enough Life Insurance to either pay off debts, generate a regular income, or both.

9. Conditions of release under the SIS Act – there are particular conditions when money can be released from superannuation (death, terminal illness, permanent incapacity, temporary incapacity, etc.). There are particular conditions within insurance contracts that may not meet a condition of release under the SIS Act such as own occupation TPD and ancillary benefits under Income Protection which may force the trustee to hold the benefits within the SMSF until some other condition of release is met.

10. Age and health of the SMSF member.

11. Trust Deed – the trust deed must allow the SMSF to hold insurance. Otherwise the insurance coverage must be held outside the fund.

12. New policies after 1 July 2014 – all new Life Insurance policies issued after 1 July 2014 must align with the SIS Act and SIS Rag definitions of death, terminal illness, permanent incapacity and/or temporary incapacity.

13. Annual review – adequacy of the insurance arrangements for each member must be reviewed at the same time as the investment strategy for the fund; at least annually.

Summary

SMSF trustees have numerous issues to consider when reviewing their investment strategy, especially in relation to Life Insurance for their members. The only way for an SMSF trustee to ensure that all issues are considered in relation to Life Insurance for its members is to engage a specialist risk adviser.

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