



All things about insurance inside SMSFs

June 2020

Presenter: Seon Sweet

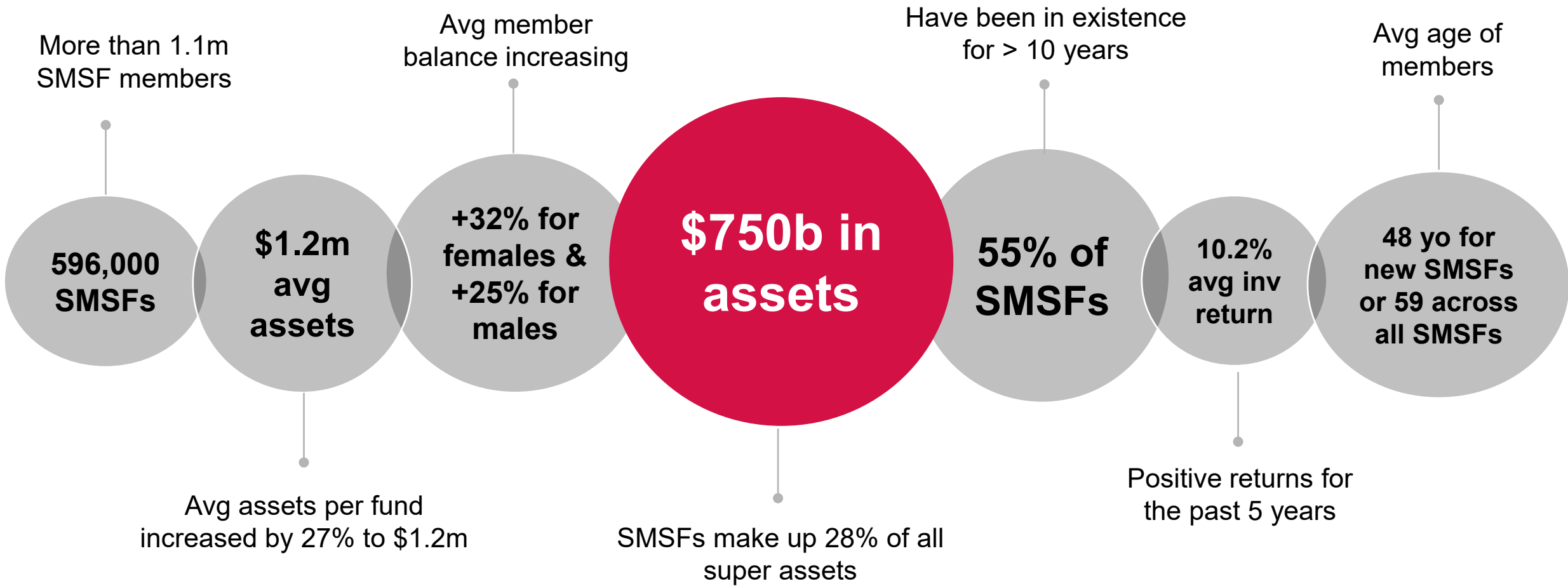


Agenda

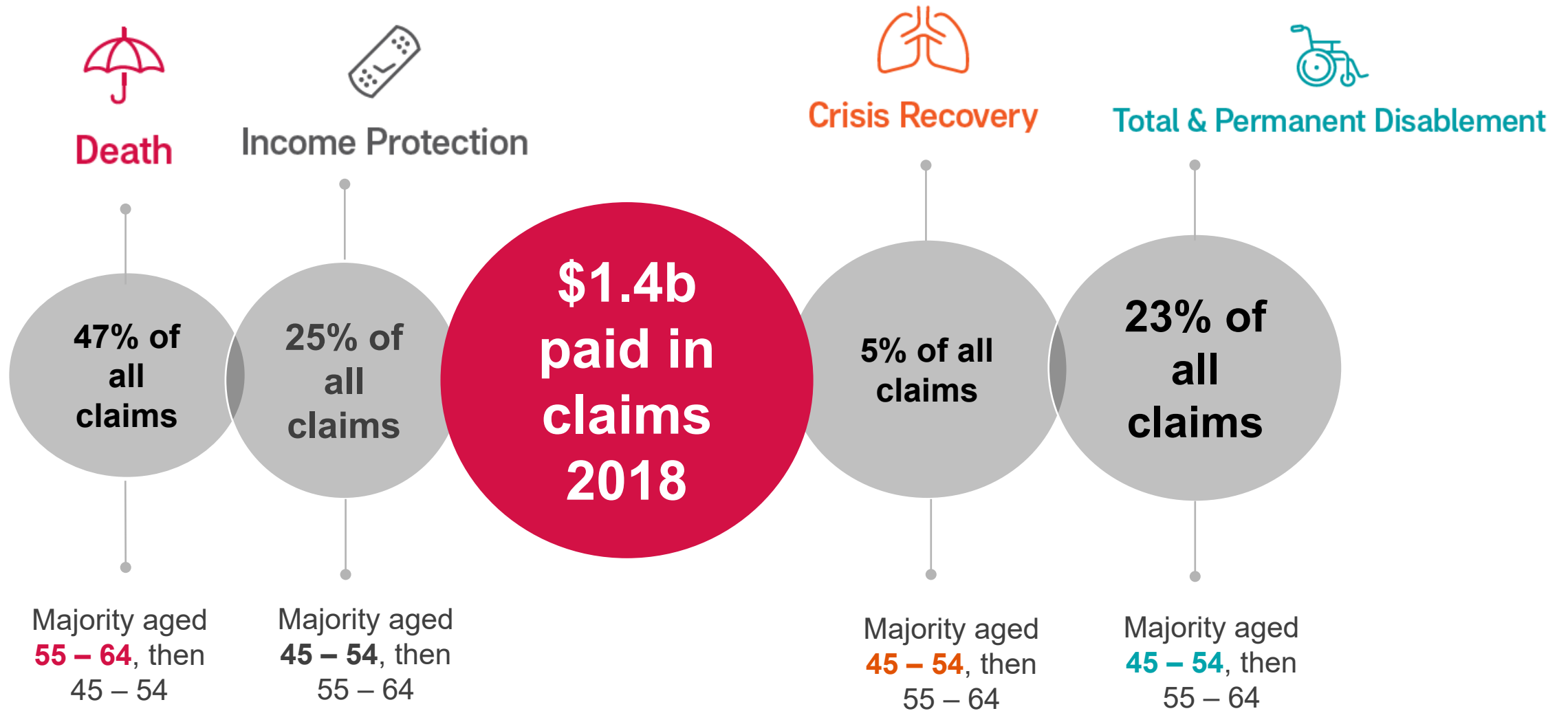
- Insurance issues to consider
- Policy ownership, premiums and proceeds
- An alternative tax deduction for premiums
- ATO view on insurance strategies



SMSF sector continues to grow



AIA 2018 claims statistics





HEALTHIER, LONGER,
BETTER LIVES



Insurance issues to consider

SMSF investment strategy requirements

SMSF trustees required to regularly review and formulate an investment strategy that gives regard to all the circumstances of the fund, including:

whether the trustees should hold a contract of insurance that provides insurance cover for one or more members of the fund

Regular review = at least annually

Penalty for breach = \$4,200 to corporate trustee or to each individual trustee (up to \$16,800)!



- ❑ Opportunity to ensure SMSF clients have addressed these requirements

Remember – restrictions on insurance in super

Type of cover	SIS condition of release	How is this met
Life	Death	Death of the 'life insured'
Terminal illness	Terminal medical condition	Two registered medical practitioners must certify that the illness or injury is likely to result in death within a 24 month period from the date of certification. At least one of the medical practitioners must be a specialist practising in an area related to the illness or injury
TPD – any occ	Permanent incapacity	The trustee is reasonably satisfied that the life insured is unlikely, because of ill health, to engage in gainful employment for which they are reasonably qualified by education, training or experience
IP	Temporary incapacity	Due to ill health, the life insured has ceased to be gainfully employed, but ill health is not permanent. Trustees can pay an income stream for no more than the member's income prior to the disablement and for a period no longer than them resuming work in their normal capacity prior to disablement



- Consider having linked / maximiser policy outside super to avoid preservation issues (TPD own occ, trauma)
- Note that IP can continue after a TPD claim in same fund!

Points to consider when determining member's insurance needs

Trustees need to prove to SMSF auditor they have considered insurance needs of members annually

Trustees may wish to consider:

- The member's age, health, assets, liabilities, income level and whether they have any dependants
- Whether the member has any existing insurance cover 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 disability

Documenting whether a member requires cover

Once issues considered, trustees should document decision in trustee minutes which:

- Acknowledge that trustees are aware of obligation to consider insurance cover
- Show trustees have considered the need for insurance cover for each member
- Documents that they have implemented cover where possible to meet needs of individual members, or
- Acknowledge that trustees have determined that insurance is, or is not, required for particular members



- Simpler to document decision in trustee minutes otherwise trustee must amend the fund's inv strategy each year
- Trustee minute should reference the fund's investment strategy to avoid any doubt

Reasons why a member may not require cover

Trustee should also document reasons why insurance cover is not required, such as:

- Members have adequate insurances in place elsewhere
- Members have significant assets in excess of liabilities (if any)
- Members happy to accept risk of being uninsured
- Members don't believe in insurance or don't want premiums impacting their retirement savings
- Trustee unable to obtain affordable life insurances due to the members' health or age

ASIC – considerations for advice providers

Advice providers must consider a client's insurance needs when recommending an SMSF

If adviser has insufficient insurance expertise to provide advice, refer client to an appropriately qualified insurance adviser

Adviser must wait until that advice is provided before recommending and establishing SMSF

Remember – insurance is a financial product. Must hold an AFSL or be an authorised representative to provide that advice

However under 'limited AFS licensee' rules, accountants can provide limited to 'class of product advice' about life risk insurance only



Key takeaways – insurance checklist

1

- Check trust deed – does it allow trustee to acquire insurances for members?

2

- Ensure trustee considers insurance needs of members annually and documents decision

3

- Ensure insurance policy definitions align with SIS condition of release

4

- Ensure policy is owned by trustee on behalf of member and paid for by SMSF

5

- Refer client/SMSF trustee to qualified insurance adviser if inexperienced or don't hold AFSL to provide advice



HEALTHIER, LONGER,
BETTER LIVES

Policy ownership, premiums and proceeds

True or false?

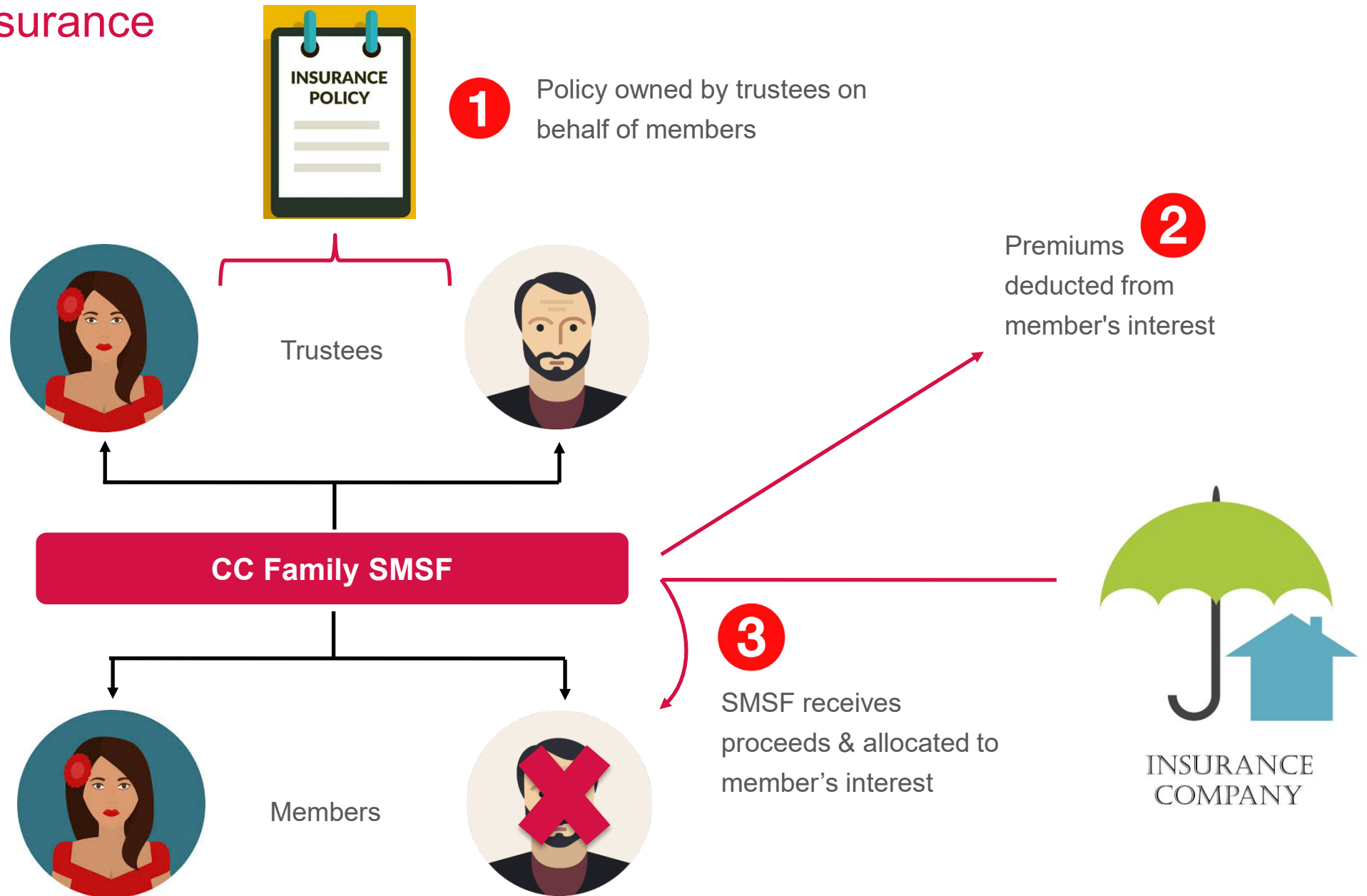
An SMSF can pay for insurance that is personally owned by a member or by trustees of another super fund.

Answer: **False**

SMSF will breach super law and regulations (e.g. providing financial assistance to members and early release of benefits) since the fund started paying the premiums (i.e. a personal expense) on their behalf.

All funds would need to be paid back to the SMSF by the SMSF member in order to rectify the contravention.

Structuring insurance in SMSF



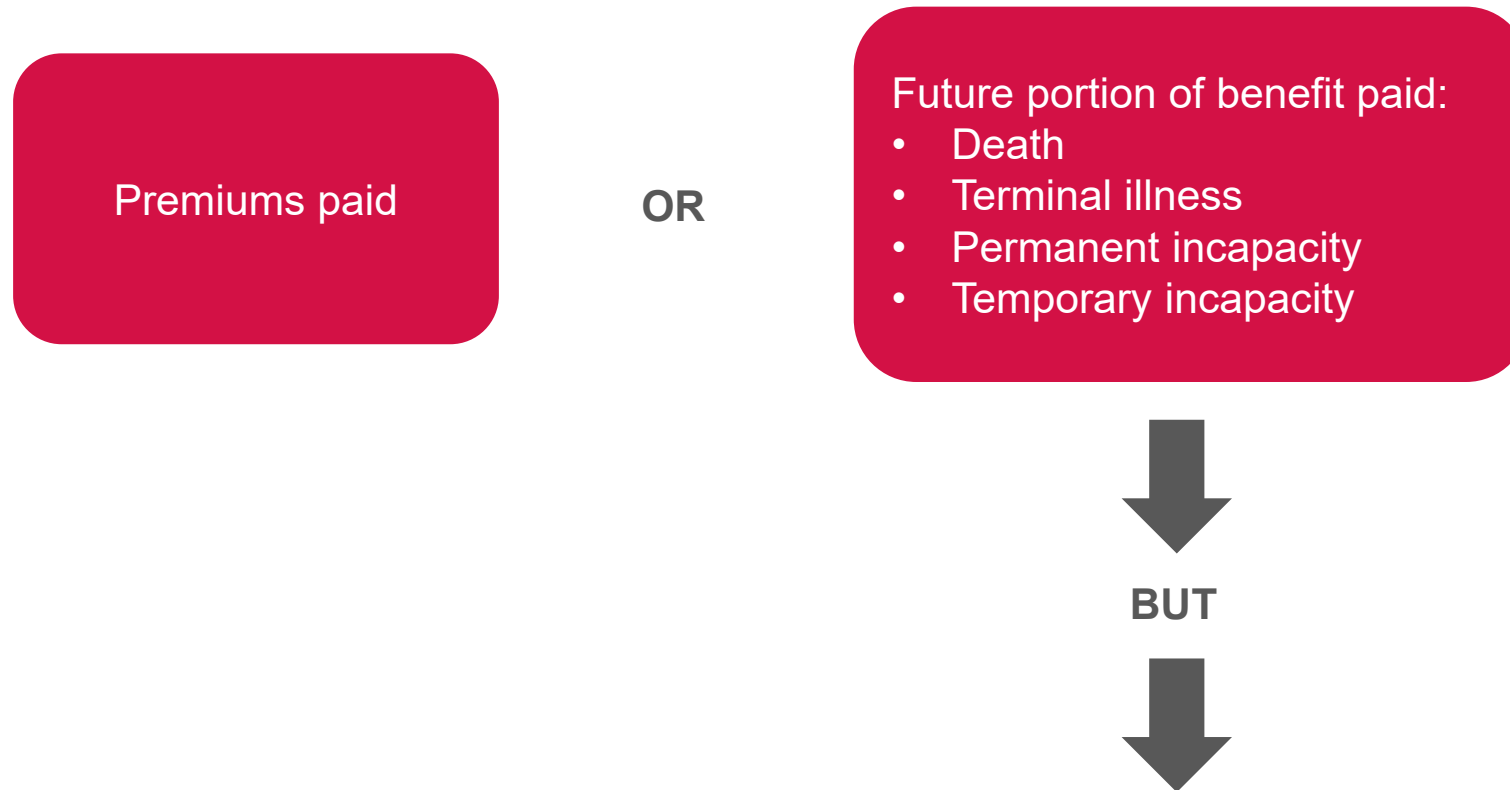


HEALTHIER, LONGER,
BETTER LIVES

An alternative tax deduction

An alternative deduction

Trustee can choose to claim a deduction for:

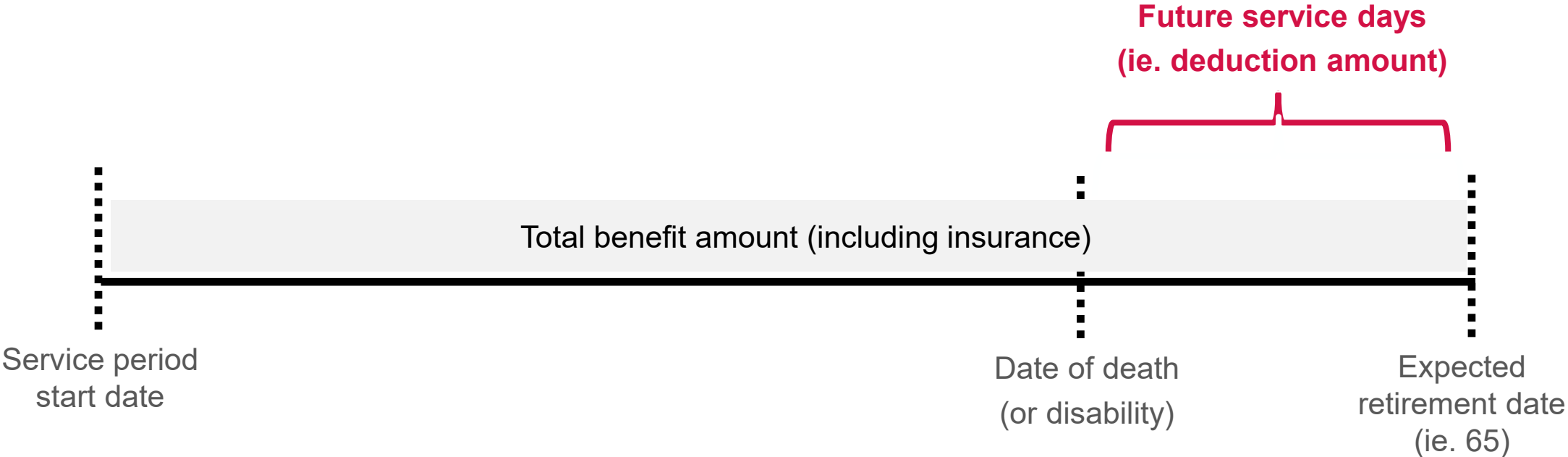


- Never again claim premium deductions
- Event must have led to termination of employment (for death & TPD benefits)

Calculate the future service deduction

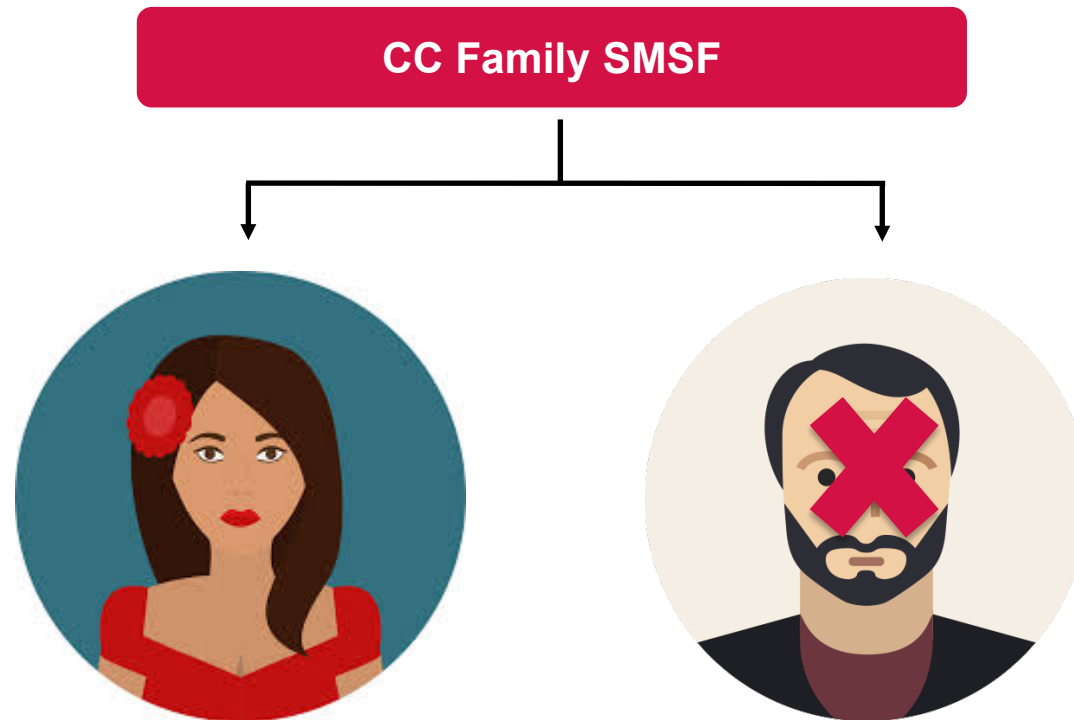
- Deductible portion of benefit:

Benefit amount x (future service days / total service days)



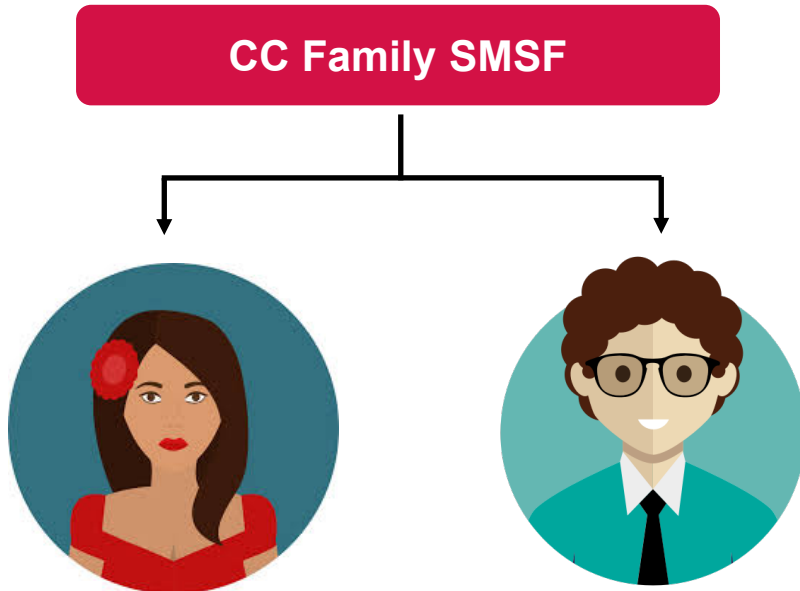
Example – future service deduction

Meet Carlos



- Carlos dies at age 50
- At time of death, his service period = 28 years
- Total death benefit (incl insurance) = \$2,450,000
- Should wife Camila claim tax deduction for premium (\$2k) or future service deduction in SMSF?

Example – future service deduction Carlos' outcome



Upon Carlos' death, adult son Cristian joins fund

Camila & Cristian decide to claim 'future service deduction' in the year of Carlos' death

$$\begin{aligned}\text{Tax deduction} &= \text{benefit amount} \times (\text{future service days} / \text{total service days}) \\ &= \$2,450,000 \times (15 \text{ years} / 43 \text{ years}) \\ &= \$854,652\end{aligned}$$

Result:

- No increase to death benefit
- No change in tax components, BUT:
 - SMSF has \$854,652 in tax deductions to offset earnings and any CGT, and
 - SMSF can carry forward tax loss to reduce taxable income in future years

Key takeaways – future service deduction

1

- Trust deed must allow it

2

- Insured person needs to be working and under age 65

3

- Decision to be made in year of benefit payment – life, terminal illness, TPD and IP

4

- Ensure fund has surviving members

5

- May not apply if choose a tax deduction for premium

6

- Once election is made, irrevocable and applies to all future years



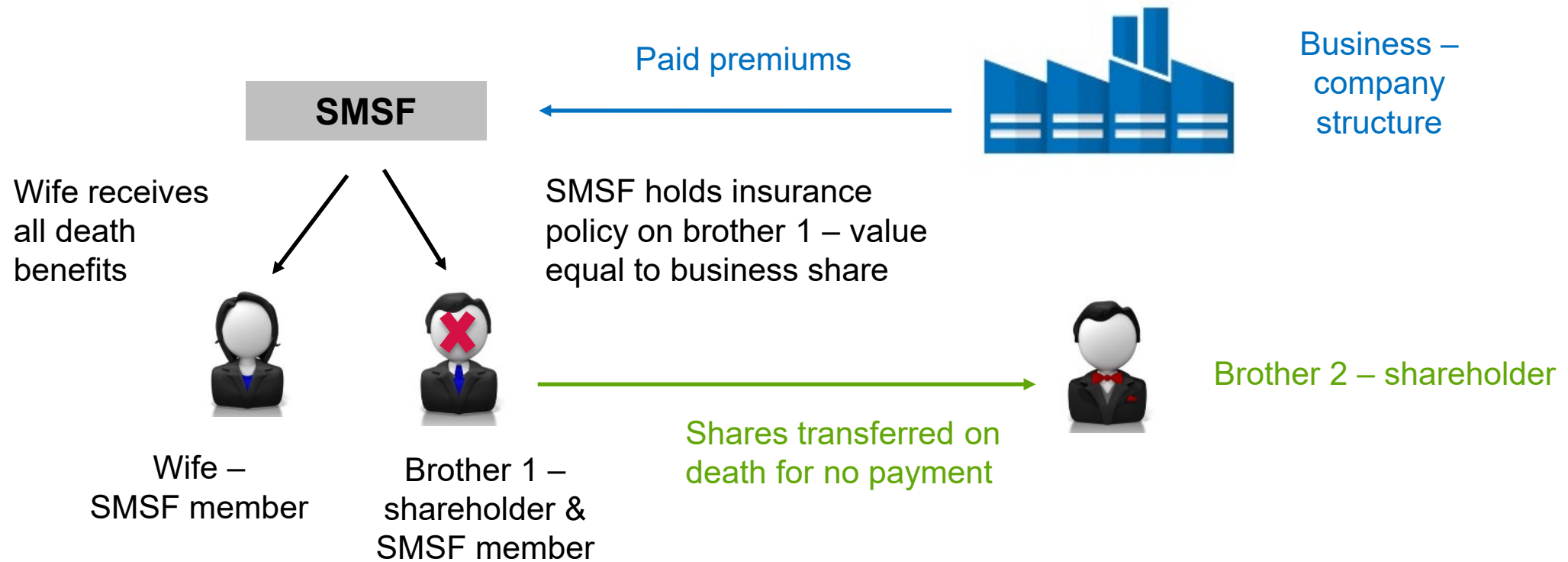
HEALTHIER, LONGER,
BETTER LIVES

ATO view on certain insurance strategies

Issue 1: business succession

The buy/sell debate

- Long been contentious whether buy/sell can be funded in super
- ATO view in ATO ID 2015/10 is that the sole purpose test was breached



Issue 1: business succession

The ATO reasoning for breach

Contravention of SIS Act:

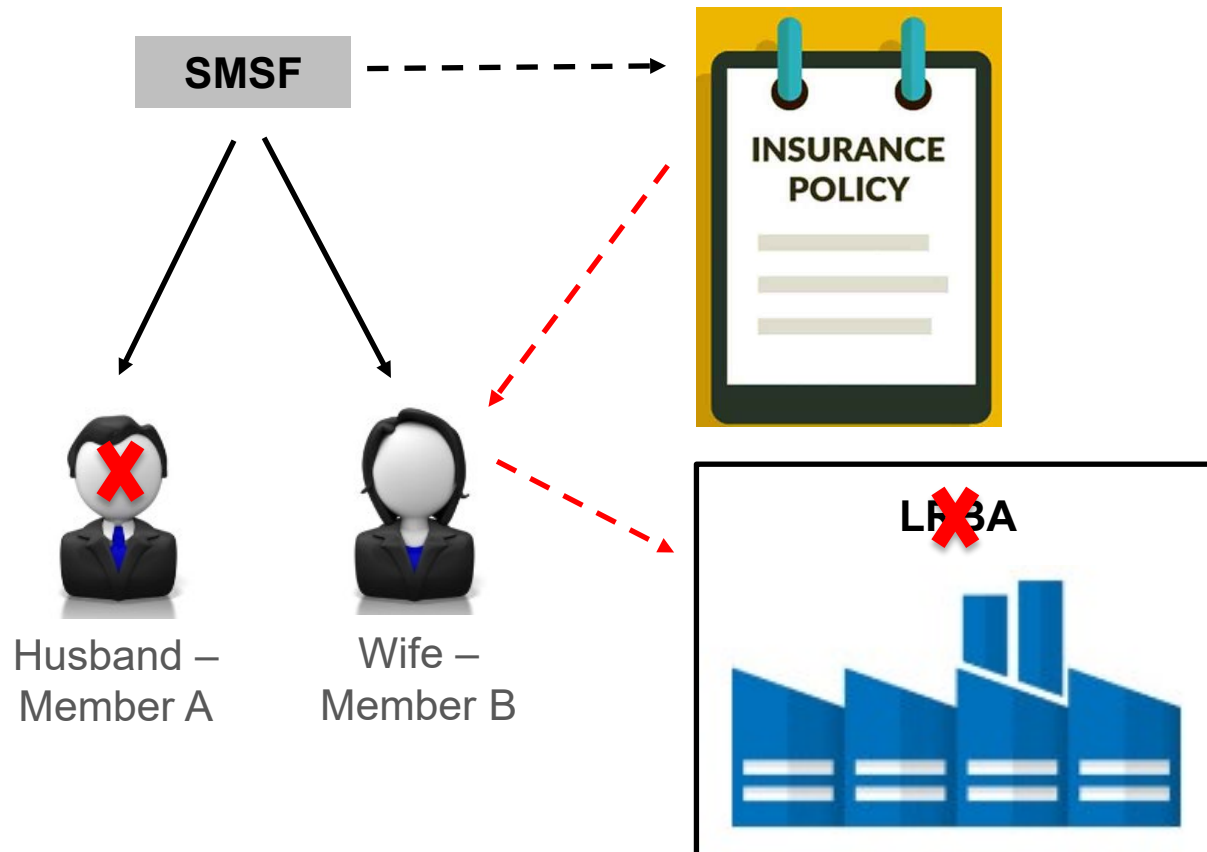
- Sole purpose test – s62 (life insurance policy was a condition and consequence of a buy-sell agreement and not related to retirement or death benefits)
- Financial assistance to a member or relative – s65 (allows 'Brother 2' to gain control of company)



- Review existing arrangements if clients are in similar situation

Issue 2: Insurance for lumpy assets

Providing liquidity to SMSFs – pre 1 July 2014



SMSF takes out insurance policy on each member

Premiums paid from:

- Other member's (non-life insured) account, OR
- SMSF reserve account

Upon death/disability, proceeds credited to that member's account / reserve account to repay debt or pay death benefit without selling asset

Issue 2: Insurance for lumpy assets

SISR and ATO view – current practice

Cross insurance and reserve strategies not permitted from July 2014

Reg 4.07D(2) of SISR 1994:

- Fund must not provide an insured benefit in relation to a member unless the insured event is consistent with a COR

ATO view (SMSFRB 2018/1):

- ATO concerned strategy is inconsistent with the SPT where purpose of policy is to satisfy other trustee obligations, eg. extinguish debt under a LRBA, rather than increase the member's interest (ie. to pay a death benefit)



- ❑ Insurance can still provide liquidity in certain circumstances

Wrap up

Consider insurance as part of SMSF investment strategy

Structure of policy ownership & allocation of premiums & proceeds is key

Alternative insurance tax deduction available!

Remember ATO views on insurance strategies

Disclaimer

Copyright © 2020 AIA Australia Limited. All rights reserved.

The content is current as at the date set out on the cover page of this presentation and may be subject to change.

This presentation provides general information only, without taking into account the objectives, financial situation, needs or personal circumstances of any individual. This presentation may contain projections concerning financial information and statements concerning future economic performance and events, plans and objectives relating to management, operations, products and services, and assumptions underlying these projections and statements. It is possible that actual results and financial conditions may differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements.

AIA Australia Limited (ABN 79 004 837 861 AFSL 230043)



HEALTHIER, LONGER,
BETTER LIVES

Thank you

Email: tece@aia.com