Insurance – Income protection insurance

Income protection insurance helps protect you by paying an ongoing income if you are unable to work due to illness or injury.

How it works

You can usually apply to protect a percentage of your earnings (e.g. 70%) for a maximum time period of your choice. For business owners, this is earnings after business expenses (which can be protected separately) but before tax. You may also be able to have an additional amount paid as contributions into your superannuation account and other ancillary benefits to help with your recovery.

The payments are taxable income, but tax may not be withheld, so you should seek tax advice and make sure you set aside money to pay your tax liabilities if this is the case. If paid through superannuation, tax is usually deducted from each payment to help you manage this obligation.

The amount you receive may also be reduced if you receive payments from sick leave, social security, workers compensation or other legislative sources.

Agreed Value or Indemnity

All new Income protection cover policies are provided under an '*Indemnity*' basis.

With an *Indemnity* policy, the amount you receive at the time of claim will usually be assessed on the basis of your earnings in the 12 months prior to the disability. Some insurers allow their *Indemnity* policies to look back further than 12 months if people have variable income (e.g. self-employed).

Indemnity policies taken out prior 1 October 2021 generally base the amount you will receive at claim on the highest 12 months of earnings in the past 2 or 3 years prior to claim. These policies may be maintained and altered at any time without losing this generous claim assessment.

Some older income protection cover policies may have been issued on an "*Agreed Value*" (AV) basis.

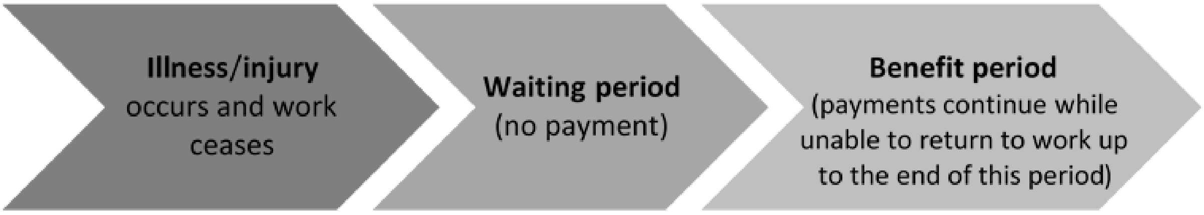
AV policies were offered until 31 March 2020 and were withdrawn from sale after this under a directive from the Australian Prudential Regulation Authority (APRA). Existing AV policies, however, may be retained and altered at any time. Under an AV policy, you will receive the agreed monthly benefit at the time of a successful claim, regardless of the amount you are earning at that time. If you hold an AV policy, it may suit you to retain it if your income fluctuates over time and you want peace of mind at time of claim.

The premium for *Indemnity* policies are less expensive than AV policies.

Waiting and Benefit Periods

In the event of a successful claim, benefit payments do not start immediately as a waiting period will apply during which no benefit is payable. The waiting period can be as short as 14 days or as long as two years. When choosing a waiting period, it's important to take into account any sick leave and related benefits provided by your employer. The shorter the waiting period, the higher the premium is likely to be.

The maximum period of time that payments continue is called the benefit period. A range of benefit periods are available - some as short as one year, with the longest continuing through to your 65th or 70th birthday. In general, the longer the benefit period, the higher the premium.



Policy Ownership

Income Protection Insurance can be owned either in your own name or within your superannuation fund.

For business owners it may be appropriate for the business to own the cover. This ensures any claim proceeds are paid directly to the business so it can distribute the funds accordingly.

Self ownership
Owning the policy in your own name may allow you to have greater control of claim payments received. With self owned cover, you pay the premium from your cash flow and generally the premiums are tax deductible. The benefits that you receive in the event of a successful claim are treated as assessable income and taxed at your marginal tax rate.

Superannuation ownership
You may also be able to purchase your income protection cover in your superannuation fund. This allows the premium to be paid from your superannuation account balance, so it does not affect your cash flow. This will reduce your retirement benefits, unless additional contributions are made to your superannuation fund to cover the cost of the premiums.

If additional contributions are made into superannuation to cover premiums, it is important to ensure you do not exceed the limits on how much can be contributed.

The premium is a tax deductible expense to your superannuation fund and can reduce the tax payable on contributions and investment income. The benefit to your account will depend on your superannuation fund.

The proceeds in the event of a successful claim are paid from your superannuation fund as a temporary incapacity benefit and will be assessable income that is taxed at your marginal tax rate.

In some circumstances, even if an insurer would otherwise pay a benefit to your superannuation fund, they may not be able to do so unless a ‘condition of release’ is met in accordance with superannuation legislation. One example is if you are not gainfully employed at the onset of the illness and injury, and another example is if you reduce working hours but do not fully cease gainful employment including paid leave such as sick leave.

Optional benefits

Income Protection policies may offer important options including:

- an Increasing Claims option that ensures benefit payments are indexed in line with inflation
- a Superannuation Cover option that allows you to have contributions made to your superannuation fund
- rehabilitation benefits.

Benefits

In the event that you cannot work due to illness or injury, income protection cover usually pays an ongoing monthly benefit for a specified period of time to help protect:

- your lifestyle by helping you to continue to meet your living expenses and debt repayments, and
- your wealth by reducing or removing the need to sell assets to generate cash.

Without income protection insurance, if you are unable to work due to illness or injury, you may need to run down your savings, sell assets, and/or rely on family or Centrelink for assistance. You may find it difficult to maintain your standard of living or pay for the care and medical assistance you need. This can place extra stress on your recovery.

Risks, consequences and other important things to consider

- Your monthly benefit could be adjusted if you receive benefits from other sources, such as benefits from other insurers, employer, worker's compensation or social security payments.
- Funding the premiums from your superannuation balance will reduce the growth of your retirement savings unless you make additional contributions to offset the premiums. These contributions will count towards your contribution caps.
- Benefits are paid monthly in arrears so your first payment would be received one month after the end of your waiting period.
- Benefit payment is usually excluded if you suffer sickness or injury as a result of war (or an act of war) or a self-inflicted act.
- Before selecting an insurance policy, you should always carefully read the Product Disclosure Statement (PDS) and policy document, and once you have selected an insurance policy, you should keep these documents in a safe place.

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