FINANCIAL DIRECTIONS

Summer 2011

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Income Protection Insurance

Cover for your way of life

If something happened to you and you were unable to work, would you have enough money set aside to cover your day-to-day bills and look after your family?

Even if you think you'd be 'okay', how long would things be okay for?

These are the questions that thousands of Australians are faced with every day. While many think 'It won't happen to me', the statistics don't lie.

It is estimated that one in three Australians will be unable to work due to illness or injury for a three-month period, or longer, during their working life*.

Confronted with this situation, many Australian families experience significant financial difficulty, sometimes with no income for more than three months.

Income protection insurance allows you to continue to receive a monthly income of up to 75 per cent of the income you were earning prior to becoming too sick or injured to work.

Income protection policies are very flexible depending on your individual circumstances, and importantly, they give you the financial security you need to be able concentrate on recovering without having to worry about your bills. Income protection can be held either within your superannuation or outside of your superannuation account.

You should check with your superannuation fund to see if it can include income protection insurance, and if the benefit offered is enough to provide you with a sufficient income in the event that something happens to you and you are unable to work.

Brendan's story

Brendan is a 32-year-old employee plumber who earns $98,100 gross income per annum. He and his wife have a $400,000 mortgage, with repayments of $2,800 a month. Brendan is very healthy and leads an active life outside of work and with a child on the way, he wanted to ensure that his family would be protected if something happened to him that made him unable to work.

Brendan did some reading on the internet but wanted professional advice about whether to buy income protection insurance through his super account or not, so he contacted his financial adviser.

Together, they decided that having income protection outside super would place him in a better financial situation, so he went ahead with an income protection insurance policy outside his super account.

While walking home from work one evening, Brendan slipped and severely twisted his knee. After obtaining medical advice, he underwent a knee reconstruction and was unable to work for about four months while his knee healed. His private health insurance was able to cover most of the medical costs, but that still left the income that family would lose while Brendan was unable to work for the four months.

Fortunately, his decision to take out an income protection insurance policy for $6,131 per month covered 75 per cent of his gross income (inclusive of all his superannuation contributions), with a 30-day waiting period.

As recommended by his financial adviser, Brendan also took out an accident option, which meant the insurer would pay him one-thirtieth of his benefit for each day that he was totally disabled, for a period of up to a month.

This payment would be backdated to the day he became disabled, with the first payment available after the first 30 days.

Since Brendan satisfied this definition, he was able to receive the full $6,131 after the first month of total disability, and $18,393.00 for the remaining three months that he was unable to work.

This meant that Brendan was able to concentrate on recovering, safe in the knowledge that his mortgage, car loan and family's lifestyle would be taken care of while he was disabled.

Can you afford not to have income protection insurance?

This case study is fictional and all figures are a guide only; they are not intended to be advice in relation to the insurance you may need.

Please check with your Sentry financial adviser to find out which income protection policy best suits your needs.

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*Source: Australian Disability Table IAD89-93 Class 2

Investing for children

Finding the best way to put money aside for your children or grandchildren needs careful thought. The bottom line is the basics of good investment should always apply.

Providing a good start in life for your family is essential to many people. Whether you're interested in starting a nest egg for a newborn or helping a grandchild save for a house, it's important to understand what investments are suitable.

When it comes to investing for children, people sometimes are too overly focused on tax issues and forget the general investment principles.

That's why it's recommended to first consider the investment time frame – how long before the funds will be needed – and then looking at the types of products and assets that will suit.

Short-term vs. long-term

So what are the options?

For short-term savings goals, say three to five years, lower risk investments such as cash and term deposits may be more suitable. A first home saver account is one option that provides a tax-effective way for people to save for their first home.

But if your sights are set on the longer term, such as an education fund for a very young child, then higher growth investments could be considered.

Your Sentry financial adviser can help you to assess the child's needs and recommend the options that suit, including shares and property. These could be held directly or in managed funds, an investment bond, or family trusts.

Buying shares or property is a popular way of providing for a child's future although it may mean that the portfolio is heavily weighted in one area and managing these investments may require some extra work.

Managed funds can be a good way of providing diversity with a single account because funds typically invest across a range of assets.

However be aware that most managed funds don't accept investments in the name of a minor (under 18 years of age) but will generally have processes to allow the investment to be set up by an adult on behalf of the child.

There's also an opportunity to set up a regular investment plan to take advantage of compounding investment returns.

Thinking about tax

After you have established the goals for your investment, tax is the next consideration. Tax rules will also play a part in the decision to place the investment in your name or the child's.

Passive investments held directly by children are taxed at very high rates. There's a reason for that. It's so that parents don't try to effectively split their income by holding investments in their children's name.

Various tax rules apply to different investments so you should check with your tax adviser for information about your own circumstances.

An investment bond combines the benefits of a managed fund with the tax benefits of a life insurance policy. It's a simple tax-effective package because investment earnings do not have to be declared in your tax return unless money is withdrawn in the first 10 years.

Establishing and maintaining a family trust can be complicated but a trust may suit some circumstances. Tax must be paid on any distributions made and any income remaining in the trust.

But the trust is able to distribute income in a way that takes advantage of the marginal tax rates of beneficiaries.

Special tax rates* apply to children under 18 who receive passive or unearned income. In general, children do not need to lodge a tax return if their only source of income is less than $416.

If the investment is in the child's name and the child has control of the investment income and any sale proceeds, then the child pays the tax. If you use the income or benefit from any sales, you are liable for any tax. This may include capital gains tax when you want to transfer the investment into the child's name.

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Deciding whether or not to place the investment in the child's name or your own essentially comes down to three factors –

- Firstly you may want to have control over it while they're young and not able to manage their money.
- Secondly, the type of investment may determine the ownership. For example super or first home saver accounts must be held in the individual's name but children may not be able to hold other investments, such as managed funds, in their own name.
- Thirdly, the various tax issues will also play a part in your decision.

Things to consider before you invest for a child

- How long before the investment will be required?
- What's the best type of product that will suit the time available?
- Should the investment be in the child's name or not?
- How will income tax affect the returns?
- What are the capital gains tax implications?

Your Sentry financial adviser can assist you to implement the most appropriate strategy for your child or grandchild.

Call today for an appointment and consultation.

*Some minors are completely exempt from the special tax rates that apply to unearned income and will continue to have their taxable income subject to adult marginal tax rates and may remain eligible for low income tax offset. They include minors in full time employment, minors with certified disabilities including where certain specified allowances or pensions are provided or minors who are double orphans.

To ensure a minor's tax obligations are met it is recommended that people seek professional taxation advice.

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Investment platforms

Like an investment supermarket, a platform gives you access to a broad list of investment products offered through many different retail fund managers at wholesale prices.

Many people choose to invest through a platform to gain access to a range of shares and managed investments, usually at wholesale prices.

What is a platform?

Platforms (sometimes called 'wraps'), master trusts or investor directed portfolio services (IDPSs) are all designed for one purpose: to simplify the administration, management and reporting of the increasingly complex portfolios investors are accumulating.

Essentially, platforms are administration facilities for investment and superannuation money. They simplify the investment process because they consolidate all the investment reporting and administration for you, and send you regular portfolio valuations and tax statements.

Benefits of the platforms

Some of the benefits of platforms include:

Choice

A platform will give you access to a range of investments across all of the major asset classes:

– shares, property, cash and fixed interest.

Depending on the product you choose, you may have anything from a limited choice of managed funds, right up to a choice of hundreds of managed funds, shares and cash options.

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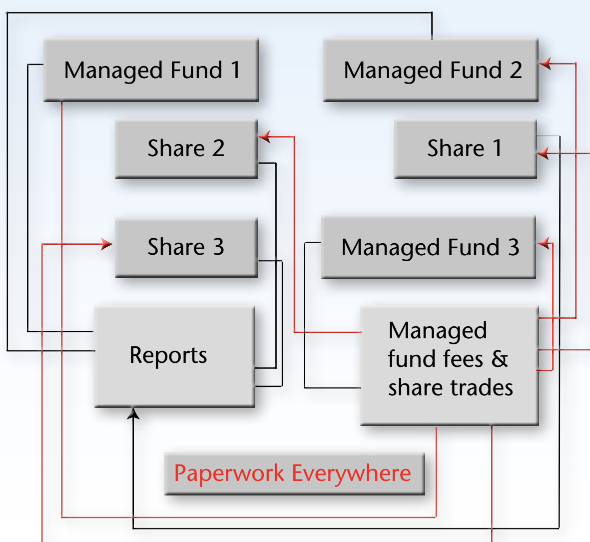
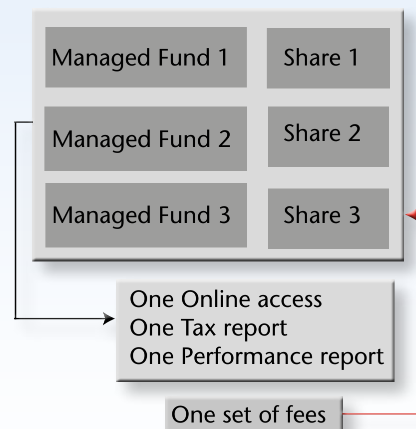
Without a platform



With a platform



Flexibility

You're in control of where your money is invested, and with your Sentry financial adviser, you can create the financial strategy that's best suited to your financial needs and goals.

Reporting

One major difference between investing through a platform and investing directly is the comprehensive and consolidated reporting provided. For example you can have 15 managed funds and 15 share investments yet receive just one regular report detailing and summarising all of your financial information.

This is particularly useful when it comes to calculating your tax. Your capital gains tax liabilities and your franking credits will be consolidated and calculated for you.

Wholesale prices

Investing through a platform often allows you access to a range of wholesale managed investments that are often not available to investors with less than $100,000 to invest.

Online access

Most platforms also give you online access to your account, so you can see how your portfolio is performing and access other information 24/7.

The benefits of diversification

Diversifying your investments means spreading them around. Many people invest across each of the main asset classes (shares, property, cash and fixed interest), and also invest in a number of securities within each asset class.

By placing your money across a number of different asset classes and investments, the negative returns you receive from one investment can offset any positive returns from another.

Whatever your financial goal, the best way to achieve your objective is to seek financial advice.

Take the time to meet with your Sentry adviser.

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For further information contact your Sentry Financial Adviser

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