TAX-EFFECTIVE STRATEGIES FOR HIGH INCOME INDIVIDUALS

COMMINSURE INVESTMENT GROWTH BOND STRATEGY PAPER

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AT A GLANCE

This paper illustrates how CommInsure's Investment Growth Bond (the CommInsure IGB) can be used to provide high income individuals with a means to increase their wealth in a tax-effective manner.

This technical paper focuses on:

- What are insurance bonds?
- CommInsure's Investment Growth Bond
- Advantages for high income individuals
- Case Study

WHAT ARE INSURANCE BONDS?

Insurance bonds, also called investment bonds ("bonds") are a flexible, tax-paid product that suits a wide range of needs and different situations. Investment bonds combine many of the features of a managed fund and a life insurance policy, with the added benefit of the investment bond provider paying 30 per cent tax on any earnings in the bond rather than an individual paying tax on earnings at their marginal tax rate.

Like a managed fund, clients can select from investment options that invest in assets such as shares, property, fixed interest and cash.

They're easy to establish and if the client has satisfied the 125% rule (where each year's contributions do not exceed 125% of the previous year's contributions) and held it for 10 years ("10 year period"), any withdrawals made will not attract personal income tax or capital gains tax. As well, the ownership of the investment can be transferred at any time without capital gains tax implications.

There is also no obligation to withdraw after the 10 year period and clients are still able to continue their investment. If a withdrawal is made during the 10 year period, all or part of the investment earnings may need to be declared in the client's tax return. The amount of tax payable on the earnings will depend on when the withdrawal is made.

The table below highlights the tax treatment of withdrawals over the 10 year period.

Time	Tax payable
Within 8 years	All earnings are taxed at client's marginal rate with a tax offset of 30 per cent
During 9th year	Two thirds of earnings are taxed at the client's marginal rate with a tax offset of 30 per cent
During 10th year	One-third of earnings are taxed at the client's marginal rate with a tax offset of 30 per cent
After 10th year	None of the earnings are taxable.

Bonds can be used to increase a client's wealth by taking advantage of the **'tax-paid'** investment feature. This makes insurance bonds particularly relevant to clients looking for strategies to grow their wealth.

COMMINSURE'S INVESTMENT GROWTH BOND

CommInsure's Investment Growth Bond has been awarded the AFA Investment Bond of the Year Award for the last 10 years running[1] and offers benefits beyond those of most investment bonds.[2]

Guarantees that protect capital from market risk

- **Investment option guarantees** are designed to provide certainty around the minimum value a client's holdings in an investment option. These are offered on four of the nine investment options. The nature of the guarantee differs across the Cash, Global Fixed Interest, Conservative and Diversified[3] investment options.
- The **Death Benefit Guarantee** provides certainty as to the minimum amount that will be paid on the death of the last surviving life insured. If the last surviving insured dies on or prior to their 99th birthday, CommInsure will pay the greater of the following amounts:
  a. The cash value of the bond,
     or
  b. The lesser of the Net Contribution Value and the Maximum Amount (the Maximum Amount is $1 million per life insured).[4]

In addition to the guarantee features described above, the CommInsure IGB offers a number of additional features.

A range of investment choices

- Suitable for a wide range of investment risk profiles with four multi-sector and five single-sector investment options.
- Switch investment options at any time with no fee and no personal capital gains tax impacts.
- Clients can tailor their own diversified portfolio from a mix of the single-sector options.

Easy investing and withdrawals

- There is a minimum initial investment of $1,000 and minimum $200 for additional contributions.
- Access to funds at any time (withdrawals may trigger a tax liability on the profit element of the investment, although clients may be able to take advantage of the 30 per cent tax offset).
- Minimum withdrawal of $1,000 ($500 for automatic withdrawals).
- Automatic withdrawal facility for balances over $10,000.

Competitive fees

- No establishment, withdrawal or switching fees.
- Management fees range from 0.85 to 1.5 per cent depending on the investment option chosen.
- Adviser Service Fees, agreed between you and your clients, may be deducted from the Bond as a one-off and/or an ongoing fee.

Investing for children

- Children as young as 10 can invest with parental/guardian consent.
- An adult can establish a Child Advancement Policy on behalf of a child under 16 years of age with the ownership of the CommInsure IGB transferring to the child at a nominated age up to 25 years.

Certainty for estate planning and wealth transfer

- Death benefits are tax-paid to a nominated beneficiary regardless of other estate planning arrangements, reducing the risk of estate disputes.[5]

Award winning

CommInsure's Investment Growth Bond has won the AFA Investment Bond of the Year award 10 years running, from 2008 through to 2017.[6]

1 AFA Investment Bond of the Year winner from 2008 through to 2017. Benchmarked on scores for financial, market and product strength factors.

2 Based on Strategic Insight's 2017 Benchmark report.

3 If you withdraw or switch units out of the investment option after they've been held by you for a minimum period (two years for Global Fixed Interest and three years for the Conservative and Diversified options), the unit price used to calculate the withdrawal or switch will be at least equal to the price at the time you were allocated those units or switched into this option. The Cash option offers a guarantee that the unit price will never fall irrespective of the length of time the CommInsure IGB has been held.

4 To qualify for the Death Benefit Guarantee, the younger Life Insured on the policy must be aged less than 85 at policy commencement. The Net Contribution Value is the total of all deposits less withdrawals during the life of the policy and less any switching fees, withdrawal fees and adviser service fees.

5 Where a beneficiary is nominated, the bond proceeds will not be subject to challenges to the client's estate, as they will not form part of the estate assets (except possibly in NSW where a bond may form part of a 'notional estate').

6 Benchmarked on scores for financial, market and product strength factors.

ADVANTAGES FOR HIGH INCOME INDIVIDUALS

- Earnings in the bond are tax-paid at the company rate of 30 percent, which is 17 percent less than the top marginal tax rate of 47 percent[7] for individuals.
- The start date of the 10 year tax period remains unchanged if the contributions in each policy year total less than 125% of the previous year's contributions.
- After the 10 year period, subject to the 125% rule being satisfied, withdrawals are free from personal income tax.
- If the earnings on a withdrawal (within the 10 years) are required to be included in assessable income, a life insurance policy tax offset of 30 per cent is available to compensate for the tax-paid by CommInsure. This may also be used to offset tax on other income.
- There is no need to declare earnings in tax returns while the money is in the bond.
- There is no obligation to withdraw after the 10 year period and clients are still able to continue their investment.
- Unlike investing directly in managed funds or shares, capital gains tax does not apply to insurance bonds, even when switching between investment options or transferring beneficial ownership of the bond.
- Unlike investing in superannuation, high income individuals are not subject to an additional 15 per cent tax on contributions.[8]
- Unlike super contribution caps and preservation rules, investment bonds generally have unlimited initial contributions with easy access to funds, making them a suitable alternative.

CASE STUDY – STRATEGY FOR HIGH INCOME INDIVIDUALS

Jennifer, 49 years

Jennifer earns $300,000 per annum and is on the top marginal tax rate of 47 percent (including two per cent Medicare levy). She is wanting to invest part of her savings, $200,000, in a tax-effective investment where she can make additional contributions. Jennifer thinks she may transfer this investment to her daughter Laila, currently aged 15, after 10 years to assist Laila in the purchase of her first home.

Jennifer's financial adviser proposes the following strategy:

Step 1

Jennifer to invest the $200,000 in the CommInsure Investment Growth Bond (IGB) invested 100 percent in the 'NC-Diversified' investment option, which has the added benefit of an investment guarantee.[1] Jennifer to also nominate her daughter Laila as the beneficiary.

Step 2

Jennifer to establish an automatic BPAY payment from her bank account to make additional contributions of $2,000 per month into the IGB to take advantage of the 125% rule.

Outcome

After 10 years, Jennifer will have invested a total of $438,000 into the IGB ($200,000 initial investment plus additional contributions of $238,000). If she does not make any withdrawals, and assuming a compounding interest rate (net of fees) of 3.92 per cent per annum[2], after 10 years the total value of her CommInsure IGB will be $590,036. And she will not have had to include any of the investment earnings in her annual tax return.

If after 10 years, Jennifer decides to transfer ownership of the IGB to Laila, the investment can be transferred without incurring any capital gains tax or personal income tax for either Jennifer or Laila. Laila will also be able to continue to accrue earnings without any additional tax liability, until she decides to use the proceeds to purchase her first home.

1 Investment option guarantee is applicable for the NC-Diversified, if the investment is held for at least three years. For eligibility criteria refer to the Product Disclosure Statement.

2 The annualized earnings rate is net of fees and taxes.

Assumptions used in preparing this strategy.

A return of 3.92 per cent per annum, is the annualised rate of return for the NC-Diversified as at 31 March 2018 and is net of fees and taxes modelled over 10 years. A tax rate of 30 per cent and management fees of 1.3 per cent have been used. Note: Investments can go up and down. Past performance is not indicative of future performance.

7 Marginal tax rate includes 2 per cent Medicare levy.

8 Refers to Division 293 tax for individuals earning $250,000 or more per annum.

For more information about how CommInsure's Investment Growth Bond could help your clients, please contact your Retirement Business Development Manager.

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