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The 'magic' of rebated insurance commissions

By Theo Marinis

I am over-insured. If I were my client, I would advise myself to have Life and Total and Permanent Disability (TPD) insurance cover of approximately $1.2M - $1.5M, CPI indexed.

Instead, my cover is around $2.7M. Should I die before age 65, this sum will help my family maintain their lifestyle without me (and then some) while the TPD cover will provide for all of us, if due to disability, I am no longer able to work.

I know that $2.7 million is more than my family needs. We are in the fortunate position of owning our home and business, with one child an adult and the other (as she often reminds me) almost an adult – but my mother was killed in a tragic car accident when I was 11. I know what it is like to barely have enough money in difficult emotional times, so I have always wanted to spare them that pain.

As a financial adviser, I should expect to be able to retire comfortably … with the key to achieving this goal by taking my own advice and making the best of the opportunities which are not always obvious. (Little wonder that one of my favourite biblical quotes is "Physician, heal thyself").

It was during this reflection over the Christmas holiday break when I was reminded of a 'not always obvious opportunity' in the form of a wealth creation strategy, which has all the potential to be overlooked – often (but not exclusively) by people who take the 'do it yourself' option.

This wealth creation strategy involves turning rebates on life insurance commissions into long-term super savings.

Ongoing Life insurance commissions paid by an insurance provider to a financial adviser are percentage based (and built in as an additional premium cost which can range from 10% and as much as 30% of the total premium) and are generally received as part of an ongoing service offering.

Payments received as commissions are required to be fully disclosed at the time the cover is established, but on-going commission payments can slip under the radar. This is particularly the case if personal insurances are not regularly reviewed.

Furthermore, as commissions increase annually in line with CPI cover and age based premium increases, over time they may end up bearing little relationship to the client service model initially agreed upon.

As a strictly 'fee for service' practice, Marinis Financial Group does not accept insurance commissions either in lieu, or as part of our fee remuneration schedule. Our clients pay a flat dollar, annual service fee based on the level of service required. Where commissions cannot be dialled down to zero (resulting in a reduction in premiums) all commission payments from providers are rebated to our clients.

The savings impact of re-investing rebated insurance commissions is demonstrated in the following example:

- Male aged 55, non-smoker
- Life and TPD sum insured: $2.7 million
- Annual premium (after full commission rebate): $18,600
- Approximate initial value of rebated commission: $7,000

In this example, which is based on my own personal insurance situation, the ongoing commission rate is approximately 25%. The initial rebated commission saving of $7,000 (which is also subject to increases in future years) is good, but not spectacular – yet.

The real value of this strategy is based on directing savings from insurance commissions to super.

Therefore, wherever possible, I recommend that my clients contribute the premiums saved on rebated insurance commissions into their superannuation fund as Concessional (Tax Deductible) Contributions.

The impact of the $7,000 rebate in the example above, will increase significantly, as (assuming a marginal tax rate of 34.5%) it effectively boosts the NET superannuation contribution by approximately $9,084 pa.

In other words, the $7,000 (after tax) premiums saved is equivalent to $10,687 gross (pre-tax CC to super) which, after 15% super fund tax, produces a NET super contribution of $9,084.

This additional $9,084 pa compounding at 7.0% pa in the superannuation environment over 10 years can generate approximately $125,500 to your super savings – for no extra cost.

If someone told me that they would give me and my family a bonus 'one hundred and twenty-five grand' in 2028, I'd be very happy!

Returning to the subject of family, I should point out that up until recently my wife Julie – also joint owner of our business – was similarly over-insured. We had also established for Julie, identical personal insurance cover for Life and TPD of $2.7M plus a separate joint Trauma insurance policy. The exception was Income Protection insurance, as we had decided that her replacement salary income could be funded via dividends from the company, if necessary.

We've since reduced Julie's cover to $1.7M. Her original cover was based on the costs of involved in raising our young children without her. Now that the children are independent, we don't need as much cover. Julie also now has significant superannuation savings, and the premium for her previous level of insurance, which increases with age, was consuming much of her concessional super contributions.

In the vast majority of cases, it is in your best financial interest to have Life insurance premiums paid through your super fund.

There are significant cost savings, averaging around (15%) per year to have life (and possibly, TPD) insurance premiums paid through a super fund, as opposed to paying premiums in an after tax out-side of super environment.

If your super is in accumulation phase and you hold life and TPD insurance (and hopefully you do, as it can provide important financial protection if disaster strikes) ask your financial adviser to re-disclose the commission payments which apply – and ask for a rebate (an option which should be available if it is truly a 'fee for service' practice).

If your adviser is not running your life insurance through your super fund, commission free, ask for an explanation – and be prepared to consider moving to an adviser who recognises the benefits.

Don't forget to include life insurance in your estate planning considerations. Any payout to a spouse or dependent child is tax free, however this is not the case for adult children or beneficiaries.

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