

# Investment Concepts – Insurance/investment bonds

An insurance bond (also called an investment bond) is a managed fund investment provided by a life company. Earnings from the bond are taxed by the life company (or friendly society) at the rate of 30%. This may be lower than your marginal tax rate.

## How it works

Insurance bonds are generally considered ‘tax paid’ investments. The life insurance company pays tax on earnings within the bond and, after 10 years, you are able to withdraw the value of the bond with no further tax payable. This makes an insurance bond a simple investment structure because there is no requirement to declare interest or capital gains in your tax return.

Withdrawals can be made from an insurance bond at any time, however you may be liable to pay some tax if a withdrawal is made within 10 years from commencement of the insurance bond.

Upon your death, the balance of your account is paid to the nominated beneficiary or your estate with no tax implications.

## Taxation

All earnings in an investment bond are taxed at the life insurance company rate of 30%. The life insurance company may also receive the benefit of franking credits and tax deductions that may reduce this effective tax rate.

No amount is included in your assessable income unless a withdrawal is made within 10 years from the date of commencement, in which case you may be eligible for a tax offset on a portion of the assessable income.

## Tax offset

If you make a withdrawal within the 10 year period, a portion of the investment growth is included in your assessable income as shown in the table below:

Withdrawal	Amount of growth included in tax return
Within 8 years	Full amount
Between 8 and 9 years	Two-thirds
Between 9 and 10 years	One-third

You are then entitled to a 30% tax offset on this assessable portion to allow for the tax already paid by the life insurance company. This offset helps to reduce your tax payable on taxable income, but cannot be used to pay the Medicare levy or be refunded as cash.

This means:

- If your marginal tax rate is higher than 30%, you will generally benefit from holding the bond for the full 10 years before making a withdrawal to take advantage of the lower tax rate.
- If your marginal tax rate is lower than 30%, you could benefit from withdrawing some or all of the bond before 10 years and as a result receive a tax offset that can reduce tax on your other income.

## **Additional contributions and the 125% rule**

Insurance bonds provide flexibility for you to make additional contributions at any time, but it is important to note that if your contributions in any year are more than 125% of the previous year's contribution, this will restart the commencement date under the 10 year rule.

For example, if you make a contribution of \$1,000 in one year, the 10 year period will recommence if the next year's contribution is more than \$1,250. However, if in one year you make no contribution, the next year's and future contributions would be \$0. In this case, contributions could still be made but the 10 year period would recommence.

## **Estate planning and insurance bonds**

An insurance bond is a life policy. The death of the life insured will trigger the payment of bond either to the nominated beneficiary or to the policy owner if no beneficiary is nominated. If the life insured is the policy owner and there is no nominated beneficiary, the balance will be paid to their estate. Any amount received as a result of the death of the life insured is completely tax-free, irrespective of the 10 year rule.

## **Centrelink assessment**

Insurance bonds are considered financial assets for Centrelink/Department of Veterans' Affairs purposes, which means the full account value is asset tested and deemed under the income test.

## **Benefits**

Some of the benefits of investing in insurance bonds may include:

- Insurance bonds are a 'set and forget' type of investment, because earnings generally do not have to be included in your tax return.
- The tax paid on your investment earnings will be less than your marginal tax rate if your marginal tax rate is higher than 30%. This may help to increase your overall return on investment and help to boost your wealth accumulation.
- Insurance bonds can provide estate planning benefits because the bond can be paid directly to a nominated beneficiary instead of having it go through your estate.
- access to a range of investment options across a range of asset classes
- can be established by parents, grandparents, godparents, uncles and aunts to provide a child with a helping hand at the start of their adult life

## **Risks, consequences and other important things to consider**

These include:

- Investing into an insurance bond can reduce your cash flow because all earnings are captured in the bond as growth.
- If the life insurance tax rate of 30% is higher than your marginal tax rate, investing into an insurance bond may result more tax being paid than if you invested into other investments.
- Withdrawals within the 10 year period that are assessable to you can impact your entitlement to certain tax offsets or other benefits or liabilities.
- Fees may be charged on investments. You should check the details in the fee section of your Statement of Advice and the Product Disclosure Statement (PDS) for your selected investment.

- The Government may change tax legislation in the future in which case it is important to review your investments to determine whether they are still appropriate for your needs and circumstances.

Version: 3.0

Issue date: 01 July 2021

**Important information:**

This document has been prepared by Actuate Alliance Services Pty Ltd (ABN 40 083 233 925, AFSL 240959) ('Actuate'), a member of the IOOF ('IOOF') group of companies ('IOOF Group'), for use and distribution by representatives and authorised representatives of Actuate, Godfrey Pembroke Group Pty Limited, Consultum Financial Advisers Pty Ltd, Bridges Financial Services Pty Limited trading as MLC Advice and Australian Financial Services Licensees with whom any IOOF Group member has a commercial services agreement.

Information in this document is of a general nature only and does not take into account your objectives, financial situation or needs. You should seek personal financial, tax, legal and such other advice as necessary or appropriate before relying on the information in this document or making any financial investment, insurance or other decision. If this document is provided to you in conjunction with a Statement of Advice ('SOA'), any personal financial advice relevant to the financial planning concept/strategy referred to in this document will be contained in that SOA.

Information in this document reflects our understanding of relevant regulatory requirements and laws etc as at the date of issue, which may be subject to change. While care has been taken in preparing this document, no liability is accepted by Actuate or any member of the IOOF Group, nor their agents or employees for any loss arising from any reliance on this document.

If any financial product is referred to in this document, you should consider the relevant PDS or other disclosure material before making an investment decision in relation to that financial product.