personal insurances

Most people purchase house, car, and health insurance without giving it much thought, but statistics show that there is often little consideration for more devastating events like death, major illness or disablement.

Have you thought about how your family or your partner would cope financially if you died? Personal insurances provide safeguard for those who depend on you from being financially distressed if you are no longer able to provide for them. We often hear people say that they cannot afford life insurance because they have so many other expenses. Unfortunately, our sad experience shows that you cannot afford not to have life insurance if it is really needed.

There are a range of insurances that are available to help you manage through difficult times. Those we recommend you consider most highly include life, income protection, trauma and total and permanent disability insurance. For business owners, key person insurance should be considered.

Personal insurances should form just one component of a comprehensive financial plan. Speak with a trusted advisor who fully understands your financial situation to help you sort out which of those insurances you need and what level of cover is appropriate and importantly within your budget.

Personal insurances at a glance

Life insurance

– pays a lump sum payout to your beneficiaries when you die.

Income protection insurance

– provides a regular payment to you should you become disabled or sick and hence unable to work for a limited period of time.

Trauma insurance

– provides a lump sum payment to you in the event that you experience an illness or injury such as heart attack or cancer.

Total and permanent disablement insurance

– pays out a lump sum in the event that you suffer a serious and significant disability that prevents you from ever working again.

Key person insurance

– a type of business insurance taken out by employers to provide a payout in the event that the business loses a key person through illness, injury or death.

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TOTAL AND PERMANENT DISABLEMENT INSURANCE

Total and permanent disablement (TPD) insurance covers you for serious and significant disability. It is usually included as part of a life insurance package and is a lump sum payment made when your doctor declares that you will never be able to work again.

It is important to examine the details of the policy, as the definition of TPD can vary markedly from one insurer to another. For example, some provide cover for disablement that prevents work in an existing job while others specify the inability to work in any job.

Premiums for TPD insurance are affected again by factors such as age, health, smoking habits and your occupation. This type of insurance can be purchased inside or outside of superannuation, but there are implications for either option which need to be considered.

You may wonder what the difference is between TPD and trauma insurance. The key difference is the fact that trauma insurance will be paid out if you suffer a medical emergency, regardless of how well you recover. However, TPD insurance will only be paid if you are unable to ever work again.

Case Study:
Having enough cover is vital

Peter and Mary are 52 and 51 respectively. They are on a plane from their home in Darwin to visit family in Melbourne, when Mary begins to feel unwell. By the time the plane lands Mary could hardly walk, and is rushed to hospital. She is diagnosed with Guillain-Barre syndrome and eventually it is determined that she could never work again and needs full-time care. The care she needs does not exist in Darwin, so the couple have to relocate their home to Melbourne. Peter must retire from his well-paid job in Darwin, many years before he'd planned, to become a full-time carer for Mary.

The couple had total and permanent disablement insurance in Mary's superannuation plan which paid out $450,000. However as they have lost income from both Mary and Peter's jobs, this was not near enough to cover their normal living expenses for many years to come in addition to the very expensive medical care that Mary required. They were forced to sell their home in Darwin and their investment property to just cover their debts.

$450,000 of cover sounds like a large amount, however long term medical bills in the absence of income mount up considerably. The decision about how much cover is required is the most difficult but the most important one you need to make. A financial planner can assist you in deciding on an appropriate level of cover.

KEY PERSON INSURANCE

Key person insurance is taken out by an employer for protection against lost revenue, profits or value of the business in the event that a key person in the business suffers from a major illness, injury or death. The key person is usually a senior executive or partner or any individual whose contribution is considered uniquely valuable to the business. This type of insurance is used by both large and small companies.

For smaller companies this insurance can be used to protect each partner. For example if one of the partners in a small firm dies, the business insurance payout would allow the surviving partners to buy the shares in the business from the family of the deceased.

In the event of losing a key person, this insurance can be used to offset the costs of hiring temporary help or recruiting a successor of the key person and losses incurred if the business cannot operate at normal capacity until a replacement is found. The amount of cover required is determined by the size of the business and the key person insured.

INCOME PROTECTION

Income protection insurance - also referred to as salary continuance - is a regular payment made to you should you become disabled or sick.

Similar to life insurance, premiums are affected by factors including your age and smoking habits and also quite significantly by the type of work you do.

Key factors influencing premiums include the waiting period, the percentage salary to be covered and the length of benefit period you want to insure.

The maximum amount that insurers will cover is 75% of salary and waiting periods will apply. The waiting period is the length of time you must be sick or unable to work before you can start claiming and while they vary, it is generally between 30 to 90 days. The waiting period should reflect your current sick leave or liquid funds you could use to meet your living costs. While this may seem like a long time to wait and therefore not worth it, consider what might happen to your family or business if you were sick for a year or longer. Payment periods generally range from one to two years or longer but will likely cease by age 65.

Income protection insurance premiums are generally tax deductible. Many employers will have income protection as part of their employee benefits, but it is important to know the scope of this cover to make sure it is right for you. Income protection insurance is essential for the self employed, those who primarily earn commission on sales, and also for wage and salary earners with limited sick leave.

Case Study:
Consider the details of your policy very carefully for your circumstances

Derek and Kim are 32 and 34 respectively. They have two children and a third on the way. Derek has a good job as a software engineer and earns $130,000 per year. Kim is currently a full-time mother. They have a $400,000 mortgage. Derek's salary meets their living expenses. Derek's superannuation is in an industry superfund where he has opted for the default insurance benefits. He isn't really sure what his policy provides for, however he assumes it is adequate cover for him and his family.

Derek is driving to work one day when a truck crosses the median strip on the M2 and collides with his car. Derek survives the crash but suffers severe injuries to his back which prevent him from sitting up. He is informed that with extensive long term physiotherapy he will eventually be able to return to work.

As Derek is not permanently disabled, the total and permanent disablement insurance will not pay out. Fortunately he does also have income protection insurance in his superfund which pays 75% of his salary. However the couple is shocked to learn that the default policy in this particular super fund only pays for a maximum of 2 years, which is unlikely to be enough in Derek's case. Had Derek given due consideration to his policy details, or had he sought advice from a financial advisor, he would have been advised to obtain a comprehensive policy that pays out until the age of 65 years. This one small detail makes a significant difference to the financial outcome for the family and demonstrates the importance of carefully reading the fine print of your policy to ensure that your cover suits your circumstances.

LIFE INSURANCE

Life insurance provides the policy beneficiary with the insurance proceeds if the insured dies.

A premium is paid for the selected level of cover and is based on the insurance company's risk: the older the person, or if the person is a smoker or pursues hazardous leisure activities, the higher the risk and the higher the premium. Your medical history will be assessed when applying for life insurance. If you have had health issues you could be refused insurance or a loading may be applied to your premium.

Life insurance can be used to pay out debts, buy the full share of a business if your partner dies, pay for funeral costs, or provide for your family after you have gone. It is a practical safeguard against financial distress but despite this, the majority of Australians are significantly under-insured or do not have any life insurance at all.

Insurance is most important for both spouses when there are dependant children. Many think that covering the mortgage is enough, but keep in mind that if that's the extent of your insurance it can put significant pressure on the surviving spouse to provide an income while looking after children and coping with their own grief. It will likely mean that the surviving spouse will have to sell the family home to pay for living and educational expenses. It could also mean that your children cannot afford to be educated in the way you had intended. As the family grows up and financial commitments change, the need for, and magnitude of, life insurance shifts.

Guardianship is another important consideration. If you have been asked to serve as guardian for your friend or family's children, consider how you might pay to raise them if there is inadequate insurance cover from their parents. While it is very flattering to be asked, are you happy to give up your plans for your own children so you can raise others who have not adequately insured themselves?

Once the need for insurance is understood and agreed, the big question then becomes - how much? There are various formulae that can be used and most take into consideration your age, the age of your dependants, your current income and lifestyle and debts, including a mortgage.

Life insurance can be purchased inside or outside of superannuation. Premiums are tax deductible inside superannuation, but on the flipside there are restrictions on how the benefits can be accessed. It is important that you have the right structure, type and amount of life insurance so discuss this with your financial planner.

Case Study:
Lack of life insurance can have long term consequences for loved ones

Unfortunately we have seen the consequences to families when someone is underinsured too often. While it is an unpleasant topic here is one example which illustrates the need.

John was 52, married to Deborah, with three children. They lived a comfortably well-off life in the Upper North Shore, with the children attending private schools, and John earning upwards of $200k per year. John unexpectedly died from a heart attack, with no life insurance. After his death, his widow learned that the comfortable life they had was entirely dependent on John's regular income. They had a $550,000 mortgage on their home, which, while manageable with John's income, after his death became an unsustainable financial burden. John's superannuation had amounted to $300,000 which was inadequate to cover all their debts and provide for Deborah and the kids' living and education expenses. While dealing with the grief for the sudden loss of their husband and father, the family had to move out of and sell the family home, relocating to a different neighbourhood, the children had to leave their friends and familiarity of their school, and Deborah had to return to work for the first time in 15 years.

The lives of John's wife and three children would have been quite different had he been covered by life insurance. A financial advisor would have advised John to secure a policy that would pay out a lump sum of approximately $2 million - sufficient to pay off the family home, provide for the education of his three children and to cover living expenses for the family until Deborah reached retirement age.

TRAUMA INSURANCE

While life insurance is very important, it must also be considered that many people don't die quickly, instead suffering from illness or injury that can last for years. Life insurance may not be of any assistance during such a scenario. Trauma insurance fills the gap. This insurance pays a lump sum in the event that you experience one of a range of specified events. There are usually between 20 and 30 'trauma events', but the vast majority pay out on the most common types: cancer, heart attack, coronary bypass surgery and stroke. These events are common, with a heart attack in Australia occurring every 11 minutes, a stroke every 10 minutes and a risk of cancer before the age of 75 years of 1 in 3.

As a general rule, trauma cover cannot be taken out within superannuation and the premiums are not tax deductible. However any lump sum payment is received tax-free. Premiums again vary according to your own circumstances.

It is important to be adequately insured for your circumstances without going so overboard that insurance premiums become an overwhelming burden. The role for trauma insurance for you and your family should be discussed with your advisor.

Case Study:
A small monthly insurance cost pays off when there are limited savings to draw on in a time of need

Amanda is 42 years old, single and renting a flat in Neutral Bay. She has a great job in marketing and is on a salary of $240,000 per annum. Amanda enjoys spending her money on her fun lifestyle, and while she has been maximising her superannuation contributions for many years, she has no savings to speak of outside superannuation.

Amanda finds a lump in her breast which turns out to be cancer, requiring a mastectomy and radiation therapy. Amanda wants to choose her doctor and hospital and so elects to be treated in the private healthcare system. While Amanda's private health insurance and Medicare cover a large portion of her medical expenses, she is left $25,000 out of pocket. As she has no cash accessible, she has no way to pay. Luckily Amanda was paying $20 a month for a trauma insurance policy providing $50,000 of cover. So with the payout Amanda can pay her medical bills, and cover her living expenses while undergoing treatment. She recovers well and returns to work after a few months with no detrimental financial impact on her life.

Trauma events covered by insurance

Typically trauma cover policies will pay benefits in the case of some or all of the following critical illnesses:

- Alzheimer's Disease
- Aplastic anaemia
- Blindness
- Burns – severe/major
- Cancer
- Cardiomyopathy
- Coma
- Coronary artery angio
- Coronary bypass surgery
- Deafness
- Dementia
- Diplegia
- Encephalitis
- Heart attack
- Heart valve surgery
- Hemiplegia
- HIV – occupational acquired
- Kidney failure – chronic
- Liver disease – chronic
- Loss of independent existence
- Loss of limbs and/or eye
- Loss of speech
- Lung disease – chronic
- Major head trauma
- Major organ transplant
- Motor neurone disease
- Multiple Sclerosis
- Paraplegia
- Parkinson's Disease
- Pulmonary hypertension
- Quadriplegia
- Stroke
- Aortic surgery
- Out of hospital cardiac arrest
- Benign brain tumour
- HIV – accidental infection
- Peripheral neuropathy

INSURANCE UNDERWRITING

When you take out insurance cover, the insurance company will want to know all about your medical history. The older you get the more likely you will have had some condition which may load up your premium or make you un-insurable. For this reason it is advisable that you start your insurances when you are young. Then, once insured you should never change insurance providers until you have been accepted by your new insurance company.

Underwriting involves you completing a personal statement on which you record all your health details. The underwriter will contact your doctor and confirm your statements. You may also be required to undertake various tests. Most of these requirements are easy to complete as most can be performed by a nurse in your home or office. Edney Ryan Wealth Management will assist you by managing this application and approval process.

It is essential that those on whom others rely financially, whether in a family or business, have adequate insurance cover. This is never more important than when starting a family or taking on a mortgage. With so many Australians under or un-insured, are you confident that you have the right protection in place? Not all insurance policies are the same and you generally get what you pay for. Edney Ryan Wealth Management can assist you to determine which insurance and how much is the right amount for your circumstances.

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