keeping an eye on finance

focus

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in this issue

Women lacking on insurance protection

When it comes to having enough insurance cover in place, there should be no 'it can't happen to me' attitude.

That's because accidents and illnesses do not discriminate, so whether you're male or female, single or married, it's equally as important to have adequate insurance in place to protect you from unforeseen events.

As logical as all that sounds, there are still many women who are very underinsured when it comes to cover for their life or a critical illness.

Getting total cover is important

While many women may take the time to shop around for health, car or home and contents insurance, important protection such as life insurance or critical illness covers are often not considered or put on the back burner.

What this means is that if they were to die suddenly, their family would receive no pay-out to cover things such as funeral expenses, outstanding debts, or to make up for the total loss of their income. In the case of a total and permanent disability, which prevented them from working, or a major critical illness, there would be no funds available to pay for long-term hospital or health care.

Without cover, some women won't be able to afford a medical specialist if they are unwell and may have to wait for treatment.

Are you single?

The Australian Bureau of Statistics has calculated that a fifth of Australia's population now live alone. Many are single women who have large debts and mortgages.

Words of Wisdom

A minute's success pays the failure of years.

Robert Browning (1812-1889)

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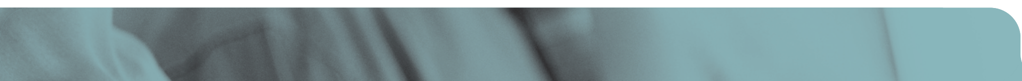


Women lacking on insurance protection (cont.)

Getting divorced, becoming widowed, or looking after adult children is getting more common for many Australian women. But many women fail to protect themselves for unforeseen illnesses if no-one is around to take care of them.

Those women who do think of life insurance usually insure their husband or partner before themselves. While this is important, more women are recognising that if they are unwell they may need money for a carer, a housekeeper, or just some money to maintain a reasonable living standard. Being unwell can be tough for your family. It can be even worse for women with children or who are on their own.

A sobering health check

Becoming critically ill is not rare. One in four women will be diagnosed with cancer of some sort in Australia, according to the Australian Bureau of Statistics.

By taking out life insurance, women can insure themselves for a fixed monthly income or lump sum payment if they become critically ill.

The amount of cover needed depends on various factors, such as age, income and debt levels.

Critical illness life insurance can pay a lump sum amount or a fixed monthly amount if a specified critical illness is suffered.

Increased awareness about cancer, screening programs and early detection means that cancer is being increasingly diagnosed in women at an earlier stage so can be more effectively treated. These types of early abnormalities are known as 'pre-invasive cancers'.

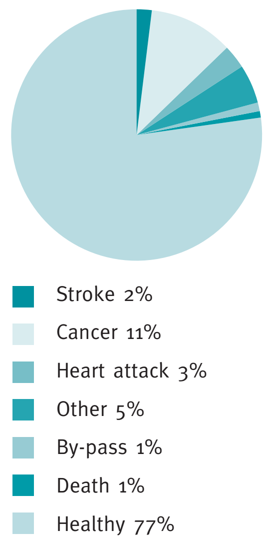
If left untreated, there is an increased risk that a mass of abnormal cells or tumour is formed and spreads to different parts of the body. These are known as malignant tumours, commonly referred to as cancer or invasive cancer, and can really bring home the potential need for life insurance for critical illness given the cost of treatment.

Seek insurance advice

If you recognise that you are underinsured, it's important to talk to us soon. We can help you find the right types of cover for your needs and to set your cover at the most appropriate level.

Are women at risk?

Women aged 36-64 are open to all sorts of critical illnesses.



Source: Pricing dread Disease Insurance, 1994: Report presented to the Institute of Actuaries of Australia, Edward Gabrizio and Warren Gratton

Reversing the retirement cash drain

It's an unfortunate reality that a high percentage of older Australian retirees do not have enough funds at hand to see them all the way through their retirement years.

Having accumulated superannuation throughout your working life, the hope is that there will be enough of an income stream post retirement to give you the sort of comfortable lifestyle you were planning on without having to go without.

Yet, having perhaps retired at age 65 with what they believed was a suitable retirement nest egg from their accumulated superannuation, many Australians are finding that 10 or 15 years down the retirement track their money pool is quickly evaporating as they try to maintain their pre retirement lifestyle.

Those that are home owners have benefited from the sharp rise in property values around the country, but despite being asset rich on paper they are poor from a cash flow perspective.

Financial institutions go into reverse

Recognising this dilemma, as average life expectancies continue to rise, an increasing number of financial institutions are offering retirees with their own home a way out from their immediate cashflow problems by lending funds that are funded via equity in their property.

Marketed as 'reverse mortgages' or home equity release loans, retirees can draw down on their home equity by taking a lump sum, a series of regular payments similar to a pension, or a combination of the two. Taking a lump sum, for instance, enables the borrower to fund a renovation plan on their home, a holiday or a new car.

The main difference between a reverse mortgage and a standard home loan is that, with a home loan, the loan balance is reduced over time and the borrower's equity will increase. With a reverse mortgages, no regular repayments are required, and interest charges are accrued on top of the loan and capitalised, increasing the size of the loan over time.

The loan, together with accrued interest, is repaid when the house is sold or the owners die. Some lenders require repayment when the borrower moves out of the property.

A retirement blessing or last resort?

There are mixed views on the merits of reverse mortgages, with most financial experts agreeing they should only be used as a last resort to supplement retirement income from pensions.

Those needing to take them may consider that even though they are withdrawing equity, the borrowed amount is being offset by the ongoing appreciation of their asset. This is correct to a degree, although rising interest rates and stagnating or falling asset prices prove that owners cannot always expect a positive return.

A general concern is the risk that as debt accumulates, because no repayments are being made, the borrower could end up owing more than the value of the home if they are not disciplined or are forced to tap into their equity relatively early in retirement and live to a very old age. Another scenario is if interest rates rise and the value of the property actually drops over time, to an extent that the borrower ends up owing more than the value of their property.

Tip

Guard against owing more than a property's value by using a reverse mortgage that offers a 'no negative equity guarantee'.

The maximum amount that can be borrowed (as a percentage of the value of the property) is substantially lower than a traditional mortgage and is determined by the age of the homeowner at the time the loan is initiated.

The older the homeowner, the more money may be borrowed, with most institutions lending up to a maximum of about 40-50 per cent for older people.

Understanding the consequences is vital

People receiving the age pension may be interested in reverse mortgages to increase income, but it is important to understand whether social security entitlements or their ability to afford aged care accommodation will be affected.

It's important to do your homework first. For example, most products come with a 'no negative equity guarantee', meaning that the value of the loan cannot exceed the value of the home. However, these can be waived if the home is not well maintained or building insurance isn't paid up.

For more information, go to the Australian Securities and Investments Commission website at www.asic.gov.au/fido and click on the Retirement income link under Products. Then click on the reverse mortgages link on the page.

If you are considering taking out a reverse mortgage, it's important that you do get advice from a qualified financial planner.

Making the salary sacrifice

We often talk about the retirement savings gap, and the need for most Australians to direct more of their income into superannuation so they can live a comfortable lifestyle once out of the workforce.

There's no doubt that a big savings gap exists, but by using salary sacrifice strategies from your work income and starting the process early, there are huge benefits that can be achieved, even by workers on average incomes.

Salary sacrifice is simply the term for using your pre-tax salary income to make voluntary contributions into superannuation in addition to superannuation guarantee payments made by your employer.

In effect, you are sacrificing some of your salary, but it may be a sacrifice well worth making.

Getting the salary benefits

If you have a high marginal tax rate – the highest being 46.5 per cent – the benefits of salary sacrificing can be substantial. As well as only having to pay 15 per cent tax on the amount sacrificed, instead of your marginal tax rate, directing the right amount into super may also:

- entitle you to certain tax offsets such as the Mature Age Worker's Tax Offset or the Low Income Earner offset
- make you eligible to receive a government co-contribution for any personal superannuation contributions you make
- reduce any impact on social security benefits you may receive

The Federal Government's announcement of another reduction in marginal tax rates in the last budget means some individuals will have less tax to save by salary sacrificing. On the other hand, because you have less tax to pay, you also have more net income available and can probably afford to salary sacrifice more into super.

Working out your net income requirements is really the first step in calculating how much gross income you can afford to salary sacrifice into superannuation.

Let's take an example of someone earning a $100,000 gross salary (net of superannuation guarantee contributions) who requires a net income of $60,000 per annum.

The following table highlights how a salary sacrifice strategy can be used to achieve this under the old tax rates and the new. The numbers show that it's possible to salary sacrifice more in the new tax regime, end up with the same income, and substantially increase your superannuation savings.

Salary sacrifice pay-off

	Pre 1 July 2006 tax rates	**2006-07 tax rates**
Salary package	$109,000	$109,000
Super guarantee	$9,000	$9,000
Salary sacrifice	$14,500	$18,200
Assessable	$85,500	$81,800
Tax	$24,210	$20,570
Medicare Levy	$1,283	$1,227
Net income	$60,008	$60,003
Net increase in super	$19,975	$23,120

As the table shows, the net increase in super is $3,145 per annum despite no drop in income.

Fact box

A low income or unemployed person with very low super may not be able to fund premiums for insurance in their super (since the premium is funded from the super balance). Where that person has a high income earning spouse, contribution splitting may enable them to fund insurance in super by the high-income earning spouse splitting their contributions to the person.

Avoiding the super rush

For people approaching 60 in particular, salary sacrificing a large amount of income often becomes a necessity to ensure there are more concessionally taxed dollars being directed into superannuation savings that will be used as a pension income stream post retirement.

Rather than waiting until the last minute, and having to live on a low budget by putting more income into super, starting earlier and salary sacrificing into super earlier will result in a higher level of retirement income without dramatically affecting your income now and without having to live on a shoestring later.

We'd be happy to discuss your salary sacrificing options with you in more detail. Please contact us to make an appointment so we can get you on the right path to retirement.

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