

# Insurance philosophy



Strategyfirst  
FINANCIAL PLANNING

Dream | Plan | Achieve

A black and white photograph showing the silhouettes of two people kayaking on a body of water. The kayakers are positioned in the middle ground, with their paddles raised. The water in the foreground is dark with gentle ripples. The sky above is filled with soft, scattered clouds, suggesting a dawn or dusk setting. The overall mood is serene and contemplative.

## **Plan** to make smart financial decisions

“Each person is different  
and therefore has different  
insurance needs”

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# Strategic thinking on insurance

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## **The Unique Human Dimension**

We recognise each person is different and, therefore, has different needs, objectives and tolerance to risks.

Our philosophy is first to understand you as an individual. Your unique circumstances and perspective towards risk will help us to design a risk management plan that best suits your objectives and needs.

## **Protecting What Matters**

Building a strategic plan to help you achieve your dreams is important. We believe protecting those dreams is equally important.

Our insurance discussions are designed to identify what measures you should take to protect yourself and your family from the financial effects of sickness, accident or death.

## **Your Best Interests**

Since inception, we have adopted a policy of avoiding conflicts of interest on all insurance policies we recommend and implement. This provides two significant benefits for you:

- 1** Lower Premiums – By removing or rebating the commissions normally charged on insurance policies, we can reduce your annual premiums by an average of 20%-30%.
- 2** Choice of Insurer – We are free to recommend whichever policy or provider we believe is most appropriate for you, without the conflicts of interest associated with commission payments.

## **Appropriate Cover**

When it comes to risk management, we want you to feel secure and have confidence in the cover you have in place. Wherever possible, we will recommend policies and features that provide the best level of cover for your situation.

## **The Right Balance**

We acknowledge that risk management can be an expensive exercise and that, in some cases, the cost of mitigating a risk may appear to outweigh the potential benefit. As such, we always strive to find the right balance between ensuring you have the best cover and the cost of obtaining this cover.

## **Tried and Tested**

Our insurance process, and the philosophy that underlies it, are designed to be as robust and practical as possible. Furthermore, based on our clients' experiences over the years (from initial discussions right through to making claims), we can honestly say the process works.



# Types of insurance cover

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There are four key types of insurance cover available to assist in your risk management plan.

**1 Life Insurance Cover**

Life insurance pays your nominated beneficiaries (including your estate) a lump-sum in the event of your death. It is generally used to repay debt and provide income to support your family.

**2 Total and Permanent Disability (TPD) Cover**

TPD insurance pays you a lump-sum if you suffer TPD or loss of independence. This cover is generally used to repay debt, provide continuing income to support you and your family, as well as funding ongoing carer costs.

**3 Critical Illness Cover**

Critical Illness or Trauma insurance provides a lump sum benefit upon suffering a defined illness. Critical Illness typically covers a range of conditions, particularly: heart attack, coronary artery bypass surgery, malignant cancer and a stroke. These account for 83% of all critical illness claims.

**4 Income Protection Cover**

If you are off work due to injury or sickness, Income Protection insurance provides a monthly benefit of up to 75% of your gross income.

You are generally considered disabled, (due to sickness or injury) if you are:

- Unable to perform at least one income-producing duty of your occupation
- Not working in any other occupation
- Under medical care.

# The right level of cover

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## Funding requirements

In order to determine the appropriate level of insurance cover, it is important to understand the outcomes you wish to achieve. While every situation is different, below are examples of some of the common assumptions we apply to our insurance calculations.

### Debt repayment

For most people, debt repayment is an important financial objective. To alleviate financial pressure on you and your family, we generally assume that upon suffering certain insurable events, you would like all debt repaid.

In some cases, it may be appropriate to only repay non-deductible debt, such as your mortgage, retaining tax-deductible debt.

### Living expenses

We assume you and your family would need sufficient capital to fund an agreed level of living expenses in today's dollars, continuing until statistical life expectancy. While our base assumption is that you would require 70% of your current expenditure, we always work with you to determine the most appropriate level of expenditure.

### Carer costs

If you become totally and permanently disabled, we assume you require a full-time Carer up until your life expectancy. We estimate the cost of this at approximately \$80,000 p.a. in today's dollars.

### Childcare

For people with young children, especially where the surviving partner continues to work, we assume a full-time Carer would need to be employed to look after your children until your youngest is 12 years old. The cost to employ a suitable person would be around \$60,000 p.a. in today's dollars.

### Education funding

We take into account the cost of funding your children's primary, secondary and tertiary education, as required. The costs will vary depending upon the desired institution or style of education.

### Best available medical care

If you were to suffer a Critical Illness, we assume you would want to be in a position to seek the best treatment, anywhere in the world.

### Replacement income

For most people their "Human Capital" (their ability to earn future income) is one of their most important assets. To protect your human capital, we assume, if you are off work due to injury or sickness, you wish to replace your lost income to the highest extent possible.

## Available resources

To prevent over-insuring, we reduce the required sum of cover by the value of resources you have available. Some common examples are outlined below:

### Existing assets

Most people have accumulated some level of assets that can be used to pay down debt and/or fund a replacement income stream. Typical assets include superannuation, investment properties (where any debt is repaid), business interests and cash.

### Continuing income

Depending on the insured event, there is often one or more income streams that will help fund the lifestyle requirements of those left behind. These include income protection benefits, your partner's earnings, ongoing business income and other sources.

### Home downsize

Another resource could be a planned downsize of the family home. This may be part of your broader objectives or a likely outcome when an insured event occurs, designed to free up capital. We can factor this in, whilst appreciating that this is not likely to be undertaken straight away.

## How are the assumptions applied?

The table below provides a guide to which assumptions generally apply to the different types of cover available.

Consideration	Life	TPD	Critical Illness	Income Protection
<b>Funding Requirements</b>				
Debt Repayment	Yes	Yes		
Living Expenses	Yes	Yes		
Carer Costs		Yes		
Childcare	Yes	Yes		
Education Funding	Yes	Yes		
Best Medical Care			Yes	
Replacement Income			Yes	Yes
<b>Available Resources</b>				
Existing Assets and Continuing Income	Yes	Yes		

The application of these assumptions can be split into two broad categories: capital items and cashflow items.

Capital items are easier to deal with, as they represent a dollar value, required today. For example, \$750,000 required to repay a home loan or \$400,000 of available assets.

Cashflow items are more complicated. We calculate a present value for any series of payments (both expenses and income) using an assumed investment return, inflation rate and time period (all based on your particular circumstances).

Once we have dollar values for all the items we wish to cover, the calculation becomes a matter of simple addition and subtraction, as illustrated in the example below.

## Example: Calculation of cover

Below is a simple example of how we calculate life insurance requirements:

Life Insurance Summary	Amount (\$)
<b>Capital Items</b>	
Debt Repayment	750,000
Less Disposable Assets	-400,000
Cover Required (A)	\$350,000
<b>Cashflow Items</b>	
Future Expenditure Required (capitalised)	2,000,000
Less Ongoing Income (capitalised)	-500,000
Cover Required (B)	\$1,500,000
Life Insurance Required (A) + (B)	\$1,850,000

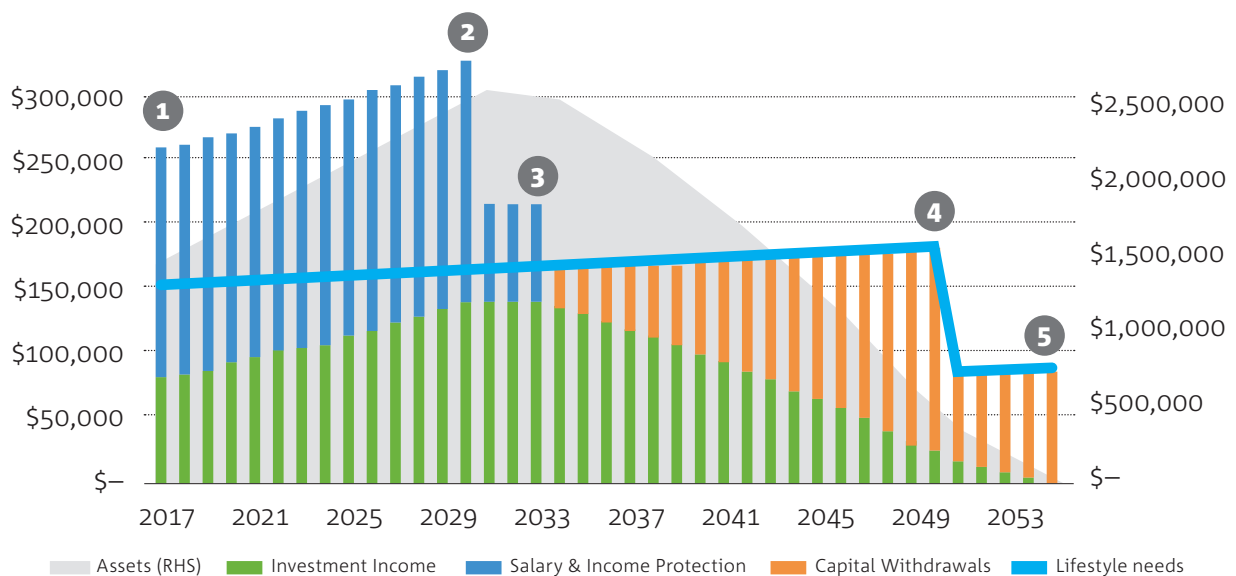
## Example: Your cover at work

After calculating your required level of insurance cover, we often end up with some imposing numbers (especially for Life and TPD cover). Even though you understand the factors we are trying to cover, it can at times be hard to understand how this relates to such a high level of insurance.

The chart below provides an example of how our recommended level of insurance (TPD in this case) meets your objectives. This example is for a couple (John and Jane), one of whom we have assumed becomes totally and permanently disabled.

### TPD funding projection

Some of the key points in time are highlighted on the chart and explained on the next page:





- 1 John is totally and permanently disabled. TPD insurance proceeds are used to repay debt and to increase asset base. Income Protection cover commences. After some time off work, Jane continues employment.
- 2 Jane retires from work. John and Jane are still generating a cashflow surplus, which can be used to build asset base.
- 3 John's Income Protection cover ceases (age 65). John and Jane now required to rely on investment assets to fund expenditure.
- 4 John dies (assuming statistical life expectancy). Carer costs are no longer required.
- 5 Jane dies (assuming statistical life expectancy). No further expenditure needs and capital is fully exhausted.

## Maintaining value

To ensure the real value of your cover is not eroded by inflation, we apply an indexation option to your policies, as a default. This will see the level of cover automatically increase each year.

# Policy ownership and features

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Once the level of cover has been determined, the next step is to consider the most appropriate ownership structure and policy features.

## Life insurance cover

### Ownership structure

You have the option to hold Life cover in your personal name or via superannuation. The choice of policy ownership will depend on several factors, such as:

- The tax treatment of the benefit payment;
- The tax deductibility of the premiums;
- The ability to direct the payment to your desired beneficiaries; and
- Your cashflow requirements.

## Total and permanent disability (TPD) cover

### Own vs. any occupation

The criteria for a successful claim depends on whether you select TPD cover based on a:

- Disability that prevents you from working in your 'own occupation'; or
- Disability that prevents you from working in 'any occupation' you are suited to by way of education, training and experience.

We generally recommend the component of your TPD cover related to repaying debt is structured with an 'own occupation' definition of disability. This means a benefit will be paid if you are unable to undertake the duties specific to your occupation.

The remaining cover will generally have an 'any occupation' definition.

### Ownership structure

While an 'any occupation' TPD policy can be held via superannuation, 'own occupation' policies generally cannot.

There are several factors we consider when determining whether to hold 'any occupation' cover via superannuation. They are identical to the factors considered for life insurance and also include:

- Whether it is appropriate to link the policy to your life cover;
- The time until you reach preservation age.

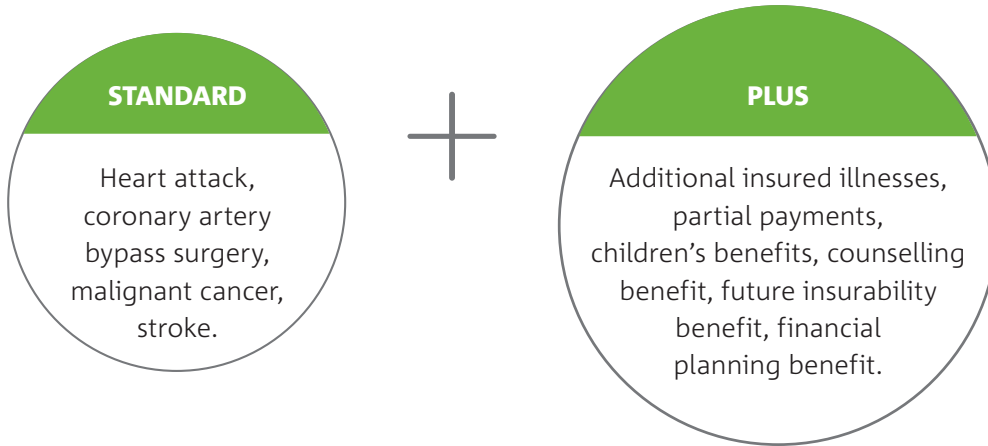
## Critical illness cover

### Ownership Structure

Suffering a critical illness may not be sufficient cause to allow money to be withdrawn from your superannuation fund. As such, Critical Illness cover is generally held in your personal name.

### Policy features

There are generally two styles of Critical Illness policies available: 'Standard' or 'Plus'. 'Plus' cover provides several additional benefits typically not available under a standard policy.



To improve the number of conditions for which you are covered, as well as the severity required before a payout, we generally recommend "Plus" style policies.

## Income protection cover

### Ownership structure

We generally recommend Income Protection cover be held in your personal name. The premium for this cover is tax deductible but in the event of a claim, the benefit is taxed as ordinary income.

### Policy features

We typically recommended 'Agreed Value' policies as opposed to 'Indemnity' policies, as the benefit under the former is guaranteed to be paid, based on your income at the time you applied for the cover.

Before a monthly Income Protection benefit is paid, there is a waiting period. Our default position is to apply a waiting period of 90-days, as this ties in with our strategic recommendation to maintain a contingency fund with at least four months' worth of expenditure. However, the waiting period can be adjusted to suit your personal needs.

Other features of your income protection policy, (e.g. the length of the benefit period and the inclusion of additional payments to cover your Superannuation Guarantee contributions), will be customised to suit your particular circumstances.

# Premium structure

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## Stepped vs. level premiums

Most insurance companies provide you with the ability to structure your premium payments on either a 'stepped' or 'level' premium basis.

Stepped premium means the cost increases each year you get older and in percentage terms, this accelerates with age.

Level premium means the cost of the cover is fixed from the outset. It will only increase if the insurance is indexed and only to an extent to cover the amount of the indexation increase.

Generally, you will have Critical Illness and Income Protection policies for the remainder of your working life. Because there is a higher probability you will make a claim on this type of cover (relative to Life and TPD cover), the annual percentage increase in stepped premium rates will rise significantly as you get older. As a result, a Level premium arrangement will provide significant long term saving.

In the case of the Life and TPD cover, because the annual percentage increase is relatively low, by the time you would generate a saving from a Level premium arrangement, you may no longer need to the cover – particularly any portion relating to debt repayment. As a result, we may recommend your Life and TPD cover are on a Stepped premium basis or are split between Stepped and Level premiums.

## Premium frequency

Most insurance companies allow you to pay your premiums on a monthly, quarterly, six-monthly or annual basis. Where possible, we recommend premiums are structured on annual basis, as this generally reduces the annual cost by 5%-7%.

## Remuneration

On all policies we recommend and implement, we remove or rebate 100% of the annual commission normally applied which generally results in premium savings of 20-30% p.a. for the life of your policies. Instead we simply charge for the time to advise, structure and implement the cover needed, for which you pay a one-off fee, agreed in advance.

By removing the commissions throughout the life of the policies and using a fee-for-service structure, you will only pay for advice when it is agreed to.

## What does this mean for you?

Across Australia 86% of personal insurance is structured on a Stepped premium basis, regardless of the potential suitability of Level premiums. Similarly, 96% of all personal insurance established in Australia is structured with commissions built into the premium.<sup>1</sup>

1. Both statistics sourced from MLC Limited.

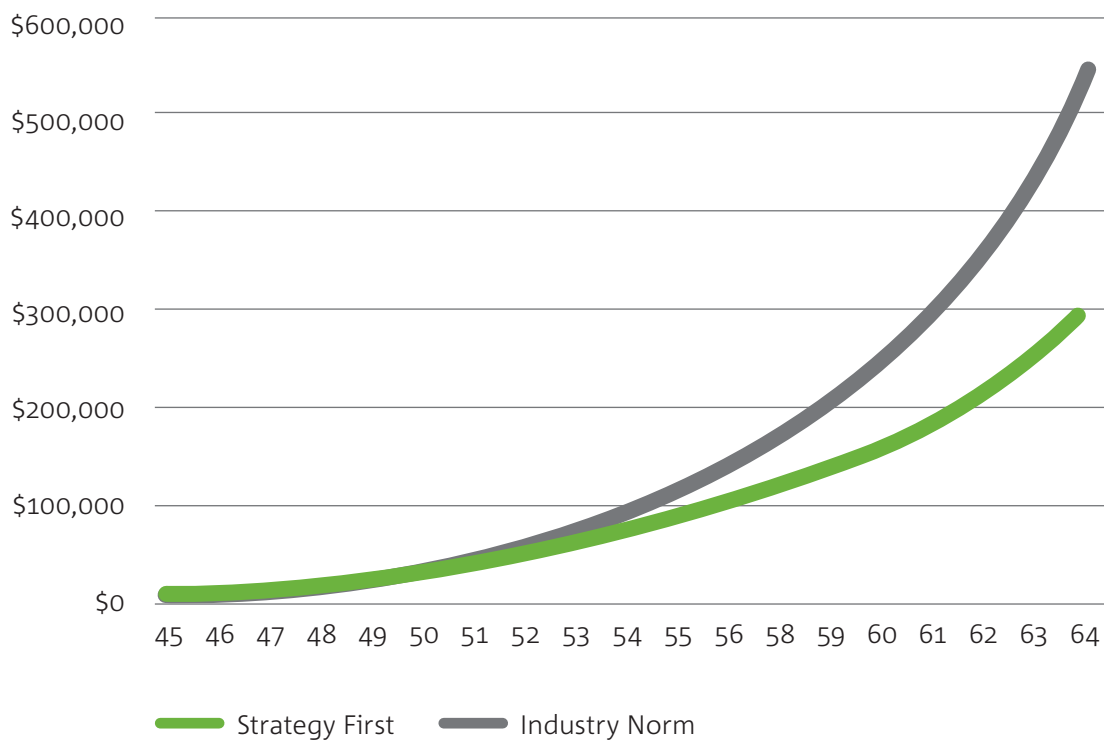
By rebating all commissions and by selecting a premium structure that is appropriate for your needs, Strategy First provides you with a significant saving, over the life of your policies.

As an example, the chart below compares the cumulative premiums for a 45-year-old male holding \$1,500,000 of life and TPD cover and \$250,000 of Critical Illness cover, under two scenarios:

- 1 The industry norm – Stepped premiums on all policies and in-built commissions of 30% p.a.
- 2 The Strategy First approach – premiums tailored to client needs and all commissions removed.

Please note, these quotes include all adviser remuneration.

### Cumulative Premiums



# Preferred insurance providers

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## Which insurance company

When determining the most appropriate insurer for your needs we assess the following:

### **Underwriting capability**

Our preferred insurers offer features such as tele-underwriting, designed to make the underwriting process as pain-free as possible. We also have dedicated underwriting teams and escalation points with our preferred insurers, which gives us an advantage when dealing with non-standard cases.

### **Claims history**

Through claims statistics and first-hand experience, we are comfortable our preferred insurers will be reliable when they are most needed: the point of a claim.

### **Product features**

Our preferred insurers rank very highly in industry-wide comparisons of product quality and features.

### **Overall financial strength**

We have confidence in the financial strength of our preferred insurers, in terms of both their life insurance arms and their parent companies.

### **Ability to remove commissions**

Our preferred insurers allow us to remove the commissions normally payable on insurance policies, resulting in a discount on your premiums of up to 30% p.a. for the life of your policies.



# Some practicalities

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## Underwriting process

When you apply to take out new cover, the insurer will analyse your information to determine if they are prepared to accept the risk of providing you with insurance.

As part of this process, you may be requested to provide additional medical information, such as blood tests, etc. Once they have completed this analysis, there are five possible outcomes:

- 1 Cover will be accepted at the standard premium rates
- 2 Cover is accepted but with an increased premium (“loading”), due to pre-existing health issue
- 3 Cover is accepted but exclusions may be applied for pre-existing illnesses, injuries or hazardous pursuits or pastimes
- 4 The proposal may be declined
- 5 A combination of 2 and 3.

During the underwriting process, we strongly recommend you do not cancel any of your existing cover until the new cover is in place. There is no guarantee the new cover will be accepted by the insurer we use. Therefore, it is vital you do not compromise your position by cancelling any existing cover during this period.

## Claims process

While the best outcome is that you never need to use your insurance, unfortunately, the statistics show some of us will in fact need it.

We understand that experiencing an insurable event is likely to be traumatic and we will do everything we can to make the process of claiming on your insurance as easy as possible. At the end of the day, we are here to help you.

Making a claim on your personal insurance typically involves several key steps:

- Step 1** Contact your Adviser and your Insurer
- Step 2** Complete your Claim forms
- Step 3** Your insurance claim is assessed
- Step 4** The outcome.

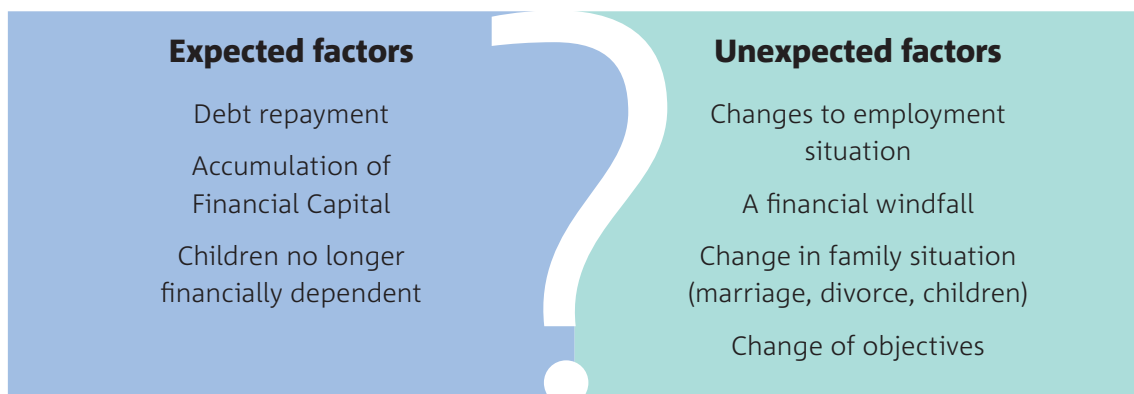
Claims payments can often be very large lump sums. We will work with you to determine the best way to deploy and manage those funds.

# A lasting relationship

## Ongoing service

Over time your need for insurance is going to change.

This might be the result of progressing towards your preferred future or it may be due to an unexpected event. Some examples of the factors that may impact your need for insurance are shown below.



It is important to regularly review your insurance cover to ensure it remains appropriate for your changing circumstances.

We implement an arrangement of ongoing review, under which we re-assess your needs, at least every two years. This review service will often form part of a broader ongoing service agreement that also includes a review of your investments and your strategic position.

The cost for the ongoing review service is structured as an annual flat-fee, agreed in advance.

# Strategyfirst

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