TPD LEVELS WHEN BUNDLING IP 5-YEAR BENEFIT PERIOD

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This higher level of TPD will provide seed capital for a long-term income stream, typically commencing from the end of the 5-year IP Benefit Period through to their 65th birthday.

The following tables illustrate the net present value (NPV) of TPD capital required to replace, on a like-for-like basis, the annual IP payments that would have otherwise been received on a 'To Age 65' IP policy for clients assuming a salary of $150,000, $200,000, and $250,000.

The NPV of TPD required has been calculated using the AIA Lump Sum Income Replacement Calculator, assuming a 7% per annum return on capital and 3% per annum indexation rate.

Did you know?

When recommending income protection with a 5-year benefit period, a higher level of TPD cover will be generally required as coverage for those illnesses that evolve into enduring and permanent ailments.

Age at beginning of IP claim	Age at end of 5-year benefit period	Years to age 65	NPV of TPD required to replace income up to 65th birthday (rounded)
	$150,000 salary		
38	43	22	$1,150,000
41	46	19	$1,050,000
44	49	16	$930,000
47	52	13	$800,000
50	55	10	$645,000
	$200,000 salary		
38	43	22	$1,500,000
41	46	19	$1,350,000
44	49	16	$1,200,000
47	52	13	$1,020,000
50	55	10	$830,000
	$250,000 salary		
38	43	22	$1,800,000
41	46	19	$1,635,000
44	49	16	$1,450,000
47	52	13	$1,240,000
50	55	10	$1,010,000

Key callouts

- The above NPV amounts would need to be grossed up if the intent is to provide immediate access to funds to retire non-deductible mortgage debt.
- It's important to take into account the net IP payments after tax. For someone earning $200,000 per annum, the insurer will replace up to 70% of income under on-sale IP contracts, or $140,000 per annum. Income tax on $140,000 per annum amounts to approximately $40,000. **Therefore, the net IP Benefit received by someone earning $200,000 is actually $100,000 per annum**. That is our reference point when determining the NPV of TPD capital required for someone earning $200,000, i.e., what NPV of TPD is required to pay a $100,000 per annum income stream for x number of years.
- If TPD claim proceeds are paid into the super fund, then used to commence a disability superannuation income stream, **three tax concessions work to make this a highly tax effective method of replacing the client's income through to age 65, which subsequently lowers the NPV of capital required**. First, the section 307-145 ITAA 1997 tax free modification calculation, which super funds are compelled to undertake if rolling over benefits to another super fund or paying a lump sum benefit, has the effect of driving a significant uplift to the tax-free component before commencing the TPD income stream. Second, the availability of the 15% pension tax offset which reduces the taxation liability on the taxable component of the pension payments. And finally, earnings on fund assets supporting the income stream accrue tax free (Transfer Balance Cap rules permitting) just like an ordinary account-based pension. In many cases, the tax-free uplift modification coupled with the 15% pension tax offset, result in the TPD pension payments being entirely tax free in the hands of the recipient.
- Some clients suffering from a permanent disablement may qualify for a Disability Support Pension, potentially taking some of the heavy lifting off the super income stream.
- The TPD claim proceeds would be funds under advice/management for the practice, thereby creating a potential additional revenue stream going forward.

AIA's IP CORE 5 or 2-year benefit period contract is underpinned by a 5-year premium rate guarantee and enduring own occupation definition of total/partial disablement.