



SUPERANNUATION

Taxation of Superannuation Death Benefits

What is a superannuation death benefit ('SDB')?

Although the most common form of SDB is a payment to a person from a superannuation fund after another person's death because the deceased was a member of the superannuation fund, various other benefits may be payable, for example payment of a superannuation annuity payment after the death of the deceased annuitant (generally superannuation income streams purchased from life insurance companies) or payments to the deceased's legal representatives of a superannuation co-contribution, or payments from Retirement Savings Accounts or Approved Deposit Funds).

Superannuation not necessarily estate asset

It must always be borne in mind that when a person dies their superannuation benefits (whether from a self managed super fund or a public fund) do not automatically form part of their estate, and are not necessarily governed by their wills.

SDB's will generally either be paid:

- 1) in accordance with a binding death benefit nomination (BDBN) left by the deceased, or
- 2) at the discretion of the trustee of the superannuation fund, to:
 - (a) a spouse or former spouse of the deceased (very widely defined, and including same sex partners since 1/7/08);
 - (b) a child (aged under 18) of the deceased;
 - (c) any person with whom the deceased had an 'interdependency relationship' just before they died;
 - (d) any person who was a 'dependant' of the deceased (generally financial dependency) just before they died.

The taxation of SDB's in the hands of the recipient depends upon the nature of the receipt.

The taxable component of an SDB is the total value of the SDB less the 'tax free component'.

The tax free component is so much of the superannuation interest as consists of:

- (a) the 'contributions segment' (contributions made since 1/7/07 that have not been included in the accessible income of the fund - eg personal contributions for which a tax deduction has not been claimed), and

- (b) the crystallised segment (if applicable) was calculated as at 1/7/07 and is equal to so much of the value of the superannuation interest immediately prior to 1/7/07 as is referable to:
- the concessional component;
 - the un-deducted contributions component;
 - the CGT exempt component;
 - the pre July 1983 component; and
 - the post June 1994 invalidity component.

A payment of an SDB is deemed to be made up of the respective proportions of taxable and tax free components as are referable to the superannuation interest from which the benefit is paid.

It is only the taxable component of the SDB which may be subject to tax. The tax free component will always be tax free in the hands of the recipient of the SDB.

Taxation of SDB's distributed to dependants

The taxation treatment of SDB's distributed to a dependant will depend on whether the benefit is received as:

- a lump sum; or
- an income stream.

Lump Sum

An SDB paid to a dependant as a **lump sum** is received tax free (whether or not the lump sum is paid from taxed or untaxed elements in the superannuation fund).

Income Stream

The taxable component of an SDB paid to a dependant as an **income stream** is tax free if either:

- 1) the deceased was aged 60 years or more at the time of their death; or
- 2) the dependant is aged 60 years or more at the time of receiving the benefit.

Such taxable component paid to a dependant is assessable income if the deceased was aged less than 60 at the time of their death and the dependant is aged less than 60 at the time of receiving the benefit (although in the later case the dependant will generally be entitled to a tax offset equal to 15% of the taxable component of the benefit [ITAA 1997 section 302 - 75]).

Regardless of the age of the deceased or the dependant any portion of the SDB referable to an amount untaxed in the fund will be assessable income and taxed at the dependant's margin rates of tax (although if the dependant or the deceased are aged 60 years or more the dependant will generally be entitled to a tax offset equal to 10% of the untaxed element [ITAA 1997 s.302-80, 85 and 90]).

An example of an untaxed element is the payment into the superannuation fund of proceeds from the deceased's life insurance policy. An SDB paid to the deceased's child as an income stream must be cashed as a lump sum when the child turns 25 (unless the child has a permanent disability). Such lump sum will generally not be taxed (SIS 1994 Reg 6.21(2B) and ITAA 1997 s.303-5), and will be treated as non assessable non-exempt income.

Taxation implications for SDB's paid to non dependants

Lump Sum

The taxable component of the SDB is included in the assessable income of the non-dependant and taxed at the non-dependant's marginal tax rate. The non-dependant will be entitled to a tax offset so that the tax rate on the amount of the SDB referable to the element taxed in the fund does not exceed 15% and the tax rate on the amount of the SDB referable to the element untaxed in the fund does not exceed 30%.

Income Stream

From 1/7/07 a non-dependant of the deceased can only receive a SDB as a lump sum, and not as an income stream.

SDB's paid to the trustee of the deceased's estate

Such SDB's will be taxed as if the benefit was paid directly to dependant or a non-dependant beneficiary of the estate.

However it is the trustee of the deceased's estate who is liable for any such tax, and not the ultimate recipient of the benefits.

The table below sets out a brief summary of the effect of the above.

SUPERANNUATION DEATH BENEFITS PAID TO DEPENDANTS			
Deceased's age	Recipient's age	Lump sum / income stream	Taxation consequence
Any	Any	Lump sum	Not assessable and not exempt (ie tax free).
Above 60	Any	Income stream	Taxable component: <ul style="list-style-type: none">■ element taxed in fund is not assessable and not exempt (ie tax free).■ element untaxed in fund is assessable income and dependant entitled to tax offset equal to 10% on that amount.
Below 60	above 60	Income stream	Taxable component: <ul style="list-style-type: none">■ element taxed in fund is not assessable and not exempt (ie tax free).■ element untaxed in fund is assessable income and dependant entitled to tax offset equal to 10% on that amount.
Below 60	Below 60	Income stream	Taxable component: <ul style="list-style-type: none">■ element taxed in fund is assessable and dependant entitled to tax offset equal to 15% of that amount.■ element untaxed in fund is assessable income.

SUPERANNUATION DEATH BENEFITS PAID TO NON-DEPENDANTS

Any	Any	Lump sum	Taxable component: <ul style="list-style-type: none">■ element taxed in fund is assessable but non-Dependant entitled to tax offset to ensure rate of tax does not exceed 15%.■ element untaxed in fund is assessable income but non-Dependant entitled to tax offset to ensure rate of tax does not exceed 30%.
Any	Any	Income stream	N/A <i>Note: Income stream benefits that commenced before 1 July 2007 will be taxed as if a Dependant.</i>

It should be noted that the Medicare Levy will also be applicable upon any superannuation death benefit where a tax rate of greater than 0% applies.

Warning

We emphasise that the comments above reflect the situation as at May 2009 and provide only a brief summary of the taxation implications of death benefit payments received from superannuation funds, highlighting some of the many issues that should be considered in planning for and making such payments, and that the tax law in relation to such payments changes from time to time.

Readers should obtain appropriate expert advice from their solicitor and accountant in relation to their particular circumstances, and not rely upon comments above in their particular circumstances.

Ensuring SDB's pass to the desired (and most tax effective) beneficiaries forms just one part of a comprehensive estate plan.

The difference between properly understanding your options and planning to ensure that your (educated) intentions are given effect to as opposed to relying on the accurate (but unhelpful) assurance that 'I'll be dead so it won't be my problem' may involve very significantly financial outcomes for loved ones.

Ken Waddington or Tracy Reeves of our office can assist you to endeavour to achieve optimal outcomes.

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