

Tricks of transferring a death benefit

DIY super
 John Wasiliev

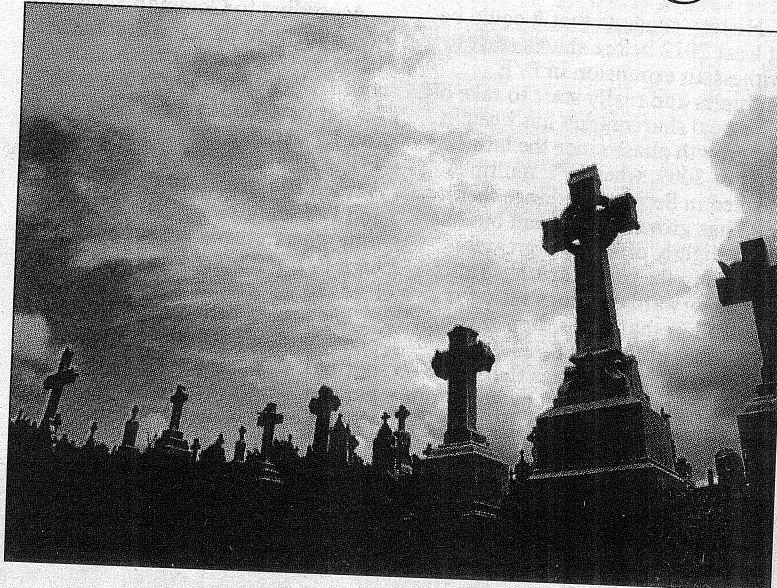
Superannuation pensions come with major tax concessions, including those paid under a death benefit arrangement. If the source of the pension is a do-it-yourself fund, the investment earnings that support the pension are tax exempt and, if the deceased member was over 60 when the pension was transferred, the income will be tax free regardless of the age of the beneficiary.

This is the scenario for a reader whose late husband passed on his super pension to her some years ago. As he was over 60, the pension income has been tax free to her, even though she is still only 53.

She recently remarried and would like to transfer her super to her new partner's fund to save on administration costs. However, she has heard there can be problems transferring a death benefit to another fund.

Pensions expert Meg Heffron, of DIY super adviser and administrator Heffron, said while normally you can't transfer a lump sum death benefit to another fund, it's a different story where the benefit is a pension.

That's because not long after the transfer, such a benefit ceases to be a death benefit and can then be an ordinary member benefit. The



Pension death benefits can be transferred to another fund. Photo: JESSICA HROMAS

actual time is either six months after death or three months after probate has been granted on the estate, whichever comes second.

So long as you wait, it is possible to transfer a benefit that started as a death benefit into another fund. You can even start a pension from this benefit, Ms Heffron said.

But there are some traps. What will be different about this new pension, as far as the reader is concerned, is that it won't necessarily be income tax free. It is only automatically income tax

free in her present situation because it is linked to her husband's death.

This link will effectively be broken by the transfer and normal super pension rules will apply, with a couple of exceptions.

One reason it won't be tax free is because she is not yet 60, when super pensions become tax free. Furthermore, the pension income could be fully taxable with no entitlement to the 15 per cent tax offset that someone who starts a pension after age 55 is entitled to.

Why there is an exception that

allows the pension to be restarted at 53 from a transferred death benefit pension, Ms Heffron said, is not just because it has become a member benefit after a relatively short period of time but also because the super is classified as a benefit that is not required to be preserved until you qualify to take it as a benefit.

Under ordinary super rules you can qualify to take a super benefit by turning either 55, when you can start a transition to retirement pension, or when you retire from full-time work.

The benefit escapes the preservation rules, Ms Heffron said, because when her husband died this satisfied a condition that released his super from the preservation rules. When someone dies, their super is reclassified as non-preserved and unrestricted as far as access is concerned.

Ms Heffron said there is a circumstance where transferring the benefit and restarting a new pension may not be as negative: where the benefit comprised mainly amounts that were not taxable.

If her late husband's super came from mostly non-concessional or after-tax contributions this would make a big difference to the income-tax treatment. This component of her inherited super will continue to be treated as a tax-free amount, even after being transferred to another fund. The income-tax

treatment will stay the same in the new fund.

Ms Heffron said that in the reader's situation the worst case would be if a big proportion of her late husband's super was a potentially taxable benefit, which would re-emerge if she transferred the money to another fund.

In this circumstance, the best strategy would be to wait until she is 60, otherwise she would give up significant tax benefits over the next seven years.

Where a large proportion of the benefit was potentially tax-free, then she should be happy to go ahead with the transfer.

A major new addition to afr.com

FINANCIAL REVIEW
DIYsuper

DIYsuper brings together the foremost experts in the superannuation field to keep you abreast of regulatory and tax changes that affect your self-managed fund and to advise you on strategies to help maximise returns.

AVAILABLE ONLINE ONLY

GO TO afr.com/diysuper