Booklet 4

Super and estate planning

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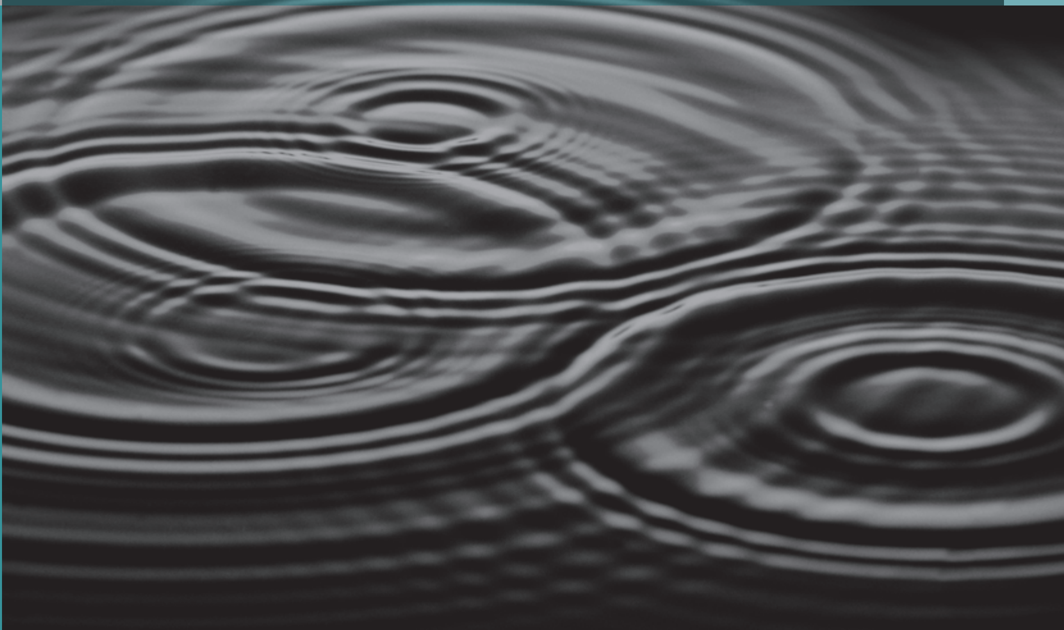

FORWARD thinking

Contents

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Introduction

Estate planning is the process of arranging your financial affairs while you are alive so that when you die, your assets pass to the people you want to receive them, in the way you intend.

Estate planning can also involve taking steps to ensure that your assets are passed on in a tax-effective manner. Superannuation is an important part of estate planning.

This booklet is the last in a series of four booklets that Macquarie Technical Services has developed to help you understand how superannuation works and to give you some tips on how you can get the most out of your super. The focus of this booklet is on the treatment of superannuation death benefits and how you can use your superannuation as an estate planning tool.

The other booklets in this series are:

- **Booklet 1: Getting the best out of your superannuation savings** which focuses on saving through super and some things to keep in mind while your super is accumulating.
- **Booklet 2: Superannuation: dealing with life's changes** which focuses on some important superannuation-related issues to consider when you experience changes in your circumstances, whether planned or unexpected.
- **Booklet 3: Account-based pensions: making your super go further in retirement** which focuses on using account-based pensions to provide income in retirement.

This series of booklets provides information about *taxed superannuation funds*. A taxed superannuation fund is a fund that pays tax on assessable contributions and investment income while benefits are accumulating. Most Australians belong to a taxed superannuation fund. We have not included information about *untaxed superannuation funds*, such as certain government or public sector funds. Different arrangements apply to these funds which are beyond the scope of these booklets.

We aim to answer some common questions people have about superannuation and how it works. But you'll probably have some questions relating to your own circumstances. If so, we recommend that you talk to your financial adviser who will be able to give you advice that is tailored to your specific needs.

In this booklet, we outline how superannuation wealth is treated on death and steps you can take to have some control over who gets your benefits and in some cases, how they are paid. We discuss some issues to consider if you want to provide for specific classes of beneficiaries including minor and adult children, and explain how you can use life insurance to top up your super death benefit. Finally, we emphasise the importance of taking an integrated approach between super and your broader estate plan.

Technical terms that are used throughout this booklet are shown in *italics* and are explained in the glossary at the end of the booklet.

Making a start

A key part of any estate plan is often a will. If you die without leaving a valid will (called dying intestate), your assets will generally be distributed to your beneficiaries as set out by law, without you having had any say over who receives them.

A will gives you control over what happens when you die and it can help to give some certainty and peace of mind for you and your loved ones.

In addition to a will, it's very important to think about what you would like to happen to your super benefits after you die. Superannuation is a very important part of estate planning and it's becoming increasingly important over time as balances grow and people choose to hold more of their wealth within super.

On your death, your super benefits may be treated differently to the other assets you own. Your benefits (including any life insurance proceeds) may not automatically form part of your estate and therefore may not be disposed of through your will. The trustee of your superannuation fund is generally required to pay your benefits either directly to your dependants or to your estate. Depending on the specific rules of your fund, you may be able to nominate to whom, and in some cases how, the trustee must pay your benefits after your death.

There are special tax arrangements for superannuation benefits paid after your death that can depend on a number of factors such as your age at death, your beneficiaries' ages, how benefits are paid and whether or not your beneficiaries are dependants for tax purposes (*tax dependants*). The treatment can also depend on the benefit's tax components and whether your death benefit includes any life insurance proceeds.

Your superannuation estate plan will need to take account of the tax arrangements and it is very important to get professional advice. Your adviser can help you to keep your plan up-to-date with changes in your circumstances and to make sure your assets are distributed in a tax-efficient way.

What happens to your superannuation benefits after your death?

After your death, the trustee of your superannuation fund is required to cash your benefits from the fund as soon as practicable either directly to one or more of your dependants (as defined under superannuation law) or your *legal personal representative* (typically referred to as your estate). Death benefits may be paid to another individual if the trustee hasn't been able to find a *legal personal representative* or a dependant of yours after making reasonable enquiries.

If paid to your estate, the proceeds from your superannuation death benefit will be distributed according to your will (assuming you have made a valid will), or the intestacy rules.

A dependant under superannuation law is known as a *SIS dependant*. A *SIS dependant* includes:

- your spouse (including a de facto);
- your child (of any age); and
- someone with whom you have an *interdependency relationship*.

In general terms, you will be taken to be in an *interdependency relationship* with someone if you have a close personal relationship with the other person, you live with them, one or each of you provides the other with financial support, and one or each of you provides the other with domestic support and personal care.

A *SIS dependant* also includes someone who is a dependant of yours within the ordinary meaning of that term, such as a person who may not be your spouse or child but who depends on you financially.

Nominating death benefit beneficiaries

Many funds will allow you to nominate one or more of your dependants or your *legal personal representative* to receive your superannuation benefits on death via a death benefit nomination. Death benefit nominations can give you control over who receives your death benefits and, depending on the rules of your fund, how they are paid. There are different types of nominations and the options available to you will depend on your fund's governing rules.

However, in some funds, the control over who receives your death benefits can rest with the trustee of your fund.

Member control

Some funds may allow members to make death benefit nominations that are binding on the trustee of a fund under superannuation law. Typically these nominations lapse after three years when you will be required to make a new nomination. Provided your nomination has not expired, meets certain conditions and your nominated beneficiary is eligible to receive your benefits, the trustee may be compelled to follow your nomination under superannuation law.

In other funds you may be allowed to make a nomination that does not lapse. If the trustee consents to your nomination, and the nominated beneficiary is eligible to receive your death benefits, the trustee may be compelled to follow the nomination under the fund's rules.

The advantage of nominations which the trustee is compelled to follow (whether three year lapsing or non-lapsing) is that you will have a high degree of certainty and control about who will receive your superannuation death benefits.

Trustee control

Not all funds allow members to make a death benefit nomination. In most of these cases, the trustee has absolute discretion in terms of who your benefits will be paid to and how they are paid (subject to requirements in the law and the fund's rules). Some funds may allow you to make a non-binding or voluntary nomination. In these cases, while the trustee may take your preference into account, they will make the final decision about who will receive your benefits, basing the decision on all relevant circumstances.

Continuing a super pension after your death

If you are receiving a superannuation pension, your fund may allow you to nominate one of your dependants (usually your spouse) who will continue to receive the pension after you die. This type of nomination is known as a *reversionary beneficiary* nomination and is usually made when you first commence a pension. There are some important restrictions that may prevent certain beneficiaries from receiving your death benefits as a pension so it's important to keep these in mind when you are making a *reversionary beneficiary* nomination. These restrictions are explained on page 6.

Keep your nomination up-to-date

You can never 'set and forget' your death benefit nomination. Regardless of what type of nomination you make, it's very important to ensure that it remains suited to your circumstances, and that your nominated beneficiary is eligible to receive your benefits (your beneficiary must be either a *SIS dependant* or your *legal personal representative)*.

For example, as your children grow older, or if you divorce and re-marry, you may wish to change the nominated beneficiary for your super death benefits.

Consider the tax implications

There can be different tax treatment depending on who receives your benefits. So when making a nomination it is important to consider the tax implications for your nominated beneficiary. The tax arrangements for superannuation death benefits are explained on the following page.

Who can receive a death benefit pension?

There are restrictions that can prevent certain beneficiaries from receiving your death benefits as a pension. A death benefit pension can only be paid to a beneficiary who is:

- a *SIS dependant* of yours other than a child;
- a dependent child of yours who is under 18;
- a child of yours under 25 who is financially dependent on you; or
- a child of yours who is permanently disabled (broadly, this is a disability that is permanent or likely to be permanent and results in the need for ongoing support and a substantially reduced capacity for communication, learning or mobility).

A death benefit paid to a beneficiary who does not meet the above criteria can only be paid as a lump sum. For example, if your death benefits are being paid to your estate, or an adult child who is not disabled or under 25 and financially dependent, they must be paid as a lump sum.

How death benefits are taxed

Recent changes to superannuation legislation have impacted on estate planning strategies involving super, particularly changes to the tax treatment of death benefits. Before 1 July 2007, death benefits, along with normal superannuation benefits, were subject to *Reasonable Benefit Limits* (RBLs). Amounts above the applicable RBL were commonly taxed at the highest marginal tax rate. The removal of RBLs from 1 July 2007 means that strategies focusing on managing excess benefits are no longer relevant and it's a good time to re-think your estate planning structures (including life insurance arrangements) within super.

The tax treatment of your death benefits can vary depending on who receives your benefit, whether your benefits are paid as a lump sum or a pension, the benefit's tax components and also whether they include any life insurance proceeds that have not been taxed in the fund.

Benefits paid to dependants are generally taxed more favourably compared to benefits paid to non-dependants. A dependant for tax purposes *(tax dependant*) has a slightly different meaning to *SIS dependant* (explained on page 4). A *tax dependant* includes:

- your spouse (including a de facto);
- your former spouse (if any);
- your child under the age of 18; and
- someone with whom you have an *interdependency relationship* (explained on page 4).

Like *SIS dependant*, a *tax dependant* also includes someone who is a dependant of yours within the ordinary meaning of that term, such as a person who depends on you financially.

The key differences between the two definitions are that a *tax dependant* does not specifically include an adult child (whereas a *SIS dependant* does) but it does specifically include a former spouse (whereas a *SIS dependant* does not).

These differences mean that an adult child, while being eligible to receive a death benefit directly from the trustee of your fund, will generally not qualify for the more favourable tax treatment that a *tax dependant* would receive, unless they are otherwise a dependant of yours (because for example, they are financially dependent on you). Also, a former spouse, while not being able to receive a death benefit directly from the trustee of your fund (unless they are otherwise a dependant of yours), may qualify for more favourable tax treatment (if, for example, they receive a super death benefit via your estate).

Tax free and taxable components

Your superannuation benefits typically consist of a *taxable component* and a *tax free component*. The *tax free component* generally represents *non-concessional contributions*. If you made a personal contribution and did not claim a tax deduction, it forms part of your *tax free component.*

The *taxable component* is the remainder of your benefit.

If you die while your benefits are in an accumulation account, the fund will determine the value of each of the tax components that make up your super entitlement at the time your death benefit is paid. If you die while your benefits are in a pension account, the percentage of *tax free component* that makes up your pension account was calculated at the time the pension commences. From the commencement day onwards, each payment made from your pension account, including payment of death benefits, will generally include this same percentage of *tax free component*.

Death benefit lump sums

A death benefit lump sum paid to a *tax dependant* is always tax free (technically, it's called *non-assessable non-exempt income*). It may seem confusing, but it will be tax free even if it comprises some *taxable component*.

The tax treatment of a lump sum paid to a *tax non-dependant* can depend on the tax components of the benefit, whether the benefit includes life insurance proceeds and if so, whether the premiums for the life insurance cover were claimed as a tax deduction. If the premiums for the life cover were claimed, the *taxable component* of the benefit will generally have an *untaxed element* which broadly reflects the fact that no contributions or earnings tax has been applied to the life insurance premiums. The tax rate applying to the *untaxed element* of a lump sum is therefore higher than the rate that applies to the *taxed element*.

Tax treatment of death benefit lump sums

Beneficiary	Tax free component	Taxable component
Tax dependant	Tax free	Tax free
Tax non-dependant	Tax free	Taxed element – 15% (plus Medicare levy) Untaxed element – 30% (plus Medicare levy)

The *untaxed element* of your benefit (if any) is calculated using a formula that takes into account your *service period* (usually your *service period* is taken to have commenced when you first started accruing the benefits) and the number of days remaining to retirement (usually to age 65). If you had *pre-July 1983 service*, and your benefit includes an *untaxed element*, the *tax free component* of your death benefit may be increased. Your adviser will be able to help you work out what these amounts might be.

Example 1: Calculating the untaxed element

Kurt passed away in 2008 at the age of 48. At the time of his death, Kurt had an accumulated superannuation balance of $200,000. He also had life insurance cover of $500,000 which is paid into his superannuation account before his superannuation death benefit is paid. His total death benefit, including life insurance proceeds, is therefore $700,000. This amount will be paid to his estate as a lump sum.

Just before his death benefit is paid, Kurt's superannuation account includes a $60,000 *tax free component*. The remainder is *taxable component*.

Kurt was born in 1960 and began accruing superannuation in 1985. Therefore, the number of years in his *service period* (from 1985 to 2008) is 23 years. The number of years remaining until Kurt would have reached age 65 (from 2008 to 2025) is 17.

Because the premiums for Kurt's life insurance cover were claimed as a tax deduction, his death benefit will include an *untaxed element* that is calculated on the following page.

Example 1 (continued):

Untaxed element = taxable component – taxed element

Broadly, the *taxed element* is calculated as follows:

$$\text{Taxed element} = \text{Amount of benefit} \times \frac{\text{Service period}}{(\text{Service period} + \text{years}^{1} \text{ to retirement})}$$

$$= \$700{,}000 \times \frac{23}{(23 + 17)}$$

$$= \$402{,}500$$

The *taxable component* of Kurt's account is $640,000 (calculated by subtracting the *tax free component* from the total value of his account). So the *untaxed element* is:

Untaxed element = $640,000 – $402,500

= $237,500

Therefore, the components of Kurt's death benefit are as follows:

Tax free component	$60,000
Taxable component – taxed element	$402,500
Taxable component – untaxed element	$237,500
Total	$700,000

If Kurt's death benefits are passed on to a *tax non-dependant* (for example, his financially independent brother), the following tax will be paid by the estate.

Tax payable by the estate

= taxed element x 15% + untaxed element x 30%

= $402,500 x 15% + $237,500 x 30%

= $60,375 + $71,250

= $131,625

[1] Days instead of years are used in the actual calculation

Lump sums paid to the estate

If a lump sum benefit is paid to the trustee of a deceased estate, the tax arrangements will depend on whether or not the beneficiaries of the estate who have benefited, or are expected to benefit, from the death benefit, are *tax dependants*.

The lump sum will be tax free to the extent that *tax dependants* have benefited, or are expected to benefit, from the death benefit.

However, the trustee of the estate will generally be required to pay tax on the death benefit to the extent that the beneficiaries, or expected beneficiaries, are *tax non-dependants*. The benefit will be taxed at *tax non-dependant* rates (but the estate is not required to pay Medicare levy) and the beneficiaries will receive the after-tax proceeds.

Anti-detriment payments

Where a death benefit lump sum is paid to your spouse, former spouse or child (including an adult child), your fund may increase the lump sum to an amount that would have been available had no tax been paid on contributions or investment earnings by the fund. The amount of the increase is often referred to as an *anti-detriment payment*.

If a lump sum death benefit is paid to your estate after your death, an *anti-detriment payment* may be available to the extent that your spouse, former spouse or child can be expected to benefit from the estate.

The *anti-detriment payment* is calculated based on the *taxable component* of your accumulated lump sum death benefit (excluding insurance proceeds). The most common way for a fund to calculate the additional payment is to use a formula accepted by the Australian Taxation Office (ATO). Essentially, for someone who joined a fund after 30 June 1988, the formula grosses up the *taxable component* of the accumulated benefits by an amount that compensates for the 15% tax deducted from contributions and investment earnings.

A fund that makes an *anti-detriment payment* is able to claim a tax deduction in the year that the payment is made. Whether or not a fund will provide an *anti-detriment payment* on top of a lump sum death benefit can depend on the fund's governing rules and also whether the fund is eligible for, and able to use, the tax deduction in that year.

Example 2: Calculating an anti-detriment payment

Marcus is aged 64 and married to Lucy aged 62. He began accruing superannuation in 1989. At the time of his death in 2008, his pension account consists of $400,000 made up of *taxable component* only. He has no life insurance held through his fund.

If a lump sum death benefit was paid to Lucy, then, based on the ATO formula, the *anti-detriment payment* will be calculated as follows:

$$\text{Anti-detriment payment} = \frac{15\% \times \$400{,}000}{85\%}$$

$$= \$70{,}588$$

Total lump sum (including anti-detriment) = $470,588

Also, Lucy will not pay tax on the lump sum because she is a *tax dependant* of Marcus.

Death benefit pensions

The tax treatment of a pension paid on death will depend on the age of the deceased when they died or the age of the beneficiary when they begin receiving the pension. If you are aged 60 or more at the time of death, or your beneficiary is 60 or more when they begin to receive a death benefit pension, payments from the pension will be tax free *(non-assessable non-exempt income)*.

However, if you are under 60 when you die, and your beneficiary is under 60, the *tax free component* of any payment will not be taxed, and the remainder (the *taxable component)* will be taxed at your beneficiary's marginal rate. However, a 15% rebate will apply.

Tax treatment of death benefit pensions

Age	Tax free component	Taxable component
Deceased or dependant aged 60 or more	Tax free	Tax free
Deceased and dependant younger than 60	Tax free	Marginal tax rates (plus Medicare levy) less 15% rebate

There are some important restrictions that prevent a beneficiary from rolling over a death benefit pension back to the *accumulation phase*, another pension or another fund, except in limited circumstances. Depending on the type of pension, there may also be a restriction on commuting the pension (to cash a lump sum). Your adviser can give you more information about these restrictions.

Providing for certain classes of beneficiaries

Dependent children

If you have children under the age of 18, there are a number of options to ensure they are adequately provided for in the event of your death. If you would like to ensure your child receives a regular stream of income, your fund may allow you to make a child pension nomination. This is a type of death benefit nomination that directs the trustee of your fund to pay all or part of your death benefits to your child as a pension. The availability of this option will depend on the rules of your super fund. An alternative to a child pension is to make provision in your will to set up a testamentary trust for your super benefits. Each of these options is explained further below. Your adviser will be able to help you work out whether either option is suitable for you.

Child pensions

If you have dependent children, your fund may allow you to nominate one or more of your children to receive your super death benefit as a pension. As explained earlier in this booklet, to be eligible to receive a child pension, at the time of your death, your child must be either:

- under 18;
- under 25 and financially dependent on you; or
- permanently disabled.

Child pensions must meet the normal payment rules for pensions, including minimum annual payment requirements, which are explained in *Booklet 3: Account-based pensions: making your super go further in retirement*. However, there are some other important restrictions in the law that apply to pensions paid to children. A child pension can't continue to be paid beyond the child's 25th birthday (and must be cashed as a lump sum – commuted – at that time), unless your child is permanently disabled. A lump sum paid in these circumstances is tax free.

In some funds, when you make a child pension nomination, you will have the opportunity to specify conditions such as:

- the level and frequency of pension payments to your child (subject to minimum payment requirements); and
- restrictions on lump sum withdrawals up to your child's specified age (subject to a maximum age of 25).

If the trustee consents to your child pension nomination, and your child is eligible to receive a pension at the time of your death, the trustee may be compelled to follow the nomination under the fund's rules.

The benefits of child pensions include:

- the payment of a regular income stream that may be structured to suit your child's needs; and
- income payments that are taxed at concessional rates. If you die at age 60 or more, a child pension will be tax free. If you are under 60 at the time of your death, the *taxable component* of a child pension will be taxed but a 15% rebate will apply. A child beneficiary will pay tax at adult marginal rates on assessable pension income rather than the punitive rates that normally apply to unearned income of minors. The combination of these concessions means that a child can receive a substantial amount of pension income before being required to pay tax. In 2008-09, assuming they receive no other income, a child could receive assessable pension payments of up to $44,211 without paying tax (but Medicare levy may still apply). A child will also have access to a tax free lump sum when the pension is eventually commuted.

Example 3: How a child pension works

Oliver has an accumulated super balance of $500,000. He and his wife Natalie have a young son Patrick, aged 10. Oliver wants to ensure that his wife and son will have a regular stream of income so they are looked after if he was to unexpectedly die. Oliver's adviser recommends using death benefit nominations for both Natalie and Patrick.

Oliver decides to make a child pension nomination for Patrick.

He would like a child pension to provide Patrick with an annual income of $15,000 (indexed by 3% per year). By the time Patrick reaches age 25, he would also like to ensure that there is approximately $50,000 (in today's dollars) left in the pension account which Patrick can receive as a tax free lump sum.

Oliver's adviser does some calculations based on an assumed earnings rate (7.5% net of fees) and works out that, if Oliver were to die this year, he would need to allocate a capital amount of $178,305 to start the child pension.

The charts on the next page show Patrick's annual pension payments and account balance over time assuming he earns investment returns of 7.5% per year.

Chart 1:

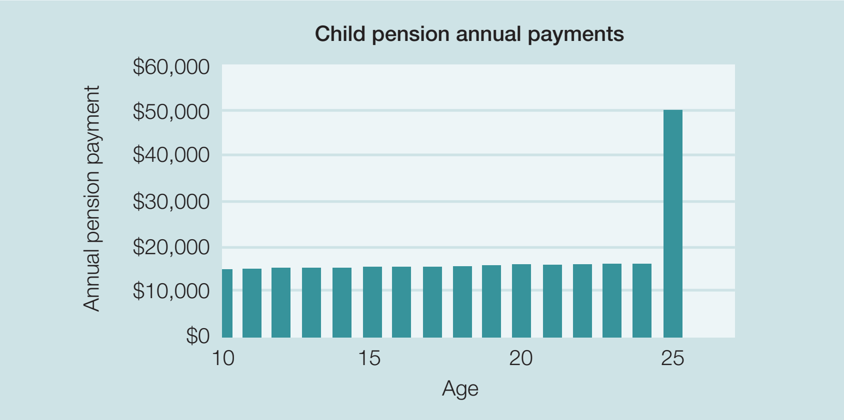
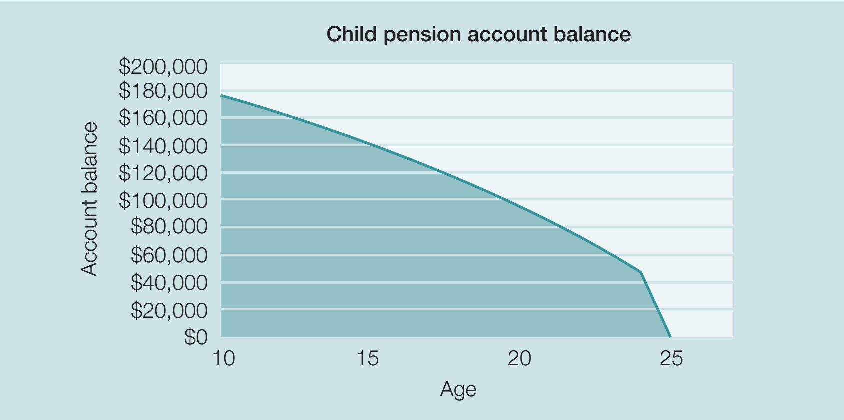


Chart 2:



Assumptions:

- all chart figures are in today's dollars (assuming the Consumer Price Index increases at the rate of 2.5% p.a.);
- payments are assumed to be made in the middle of each year;
- Chart 2 shows the account balance at the end of each year; and
- the earnings rate of 7.5% is net of fees.

Because Patrick would not be expected to receive income from any other source (at least initially), the combination of the 15% pension rebate and the low income tax offset mean that even if Oliver's death benefit was 100% *taxable component*, Patrick will not pay any tax.

Patrick makes another death benefit nomination directing the trustee of his fund to pay the remainder of his super benefits to Natalie.

Testamentary or super proceeds trusts

In providing for child beneficiaries, an alternative to a child pension is to establish a trust to distribute the proceeds of your superannuation benefits. Such a trust could either be a testamentary trust (which must be provided for under a will) or a super proceeds trust (a special trust that only accepts superannuation death benefits).

Like child pensions, child beneficiaries may be taxed at adult marginal rates rather than the punitive rates that normally apply to unearned income of minors. However, unlike a child pension paid directly from a super fund, no 15% rebate will apply.

Your financial adviser or solicitor will be able to give you more specific information about the rules that apply to each of these types of trusts.

Adult children

If you wish for your super benefits to be paid to an adult independent child, they will generally be required to pay tax on the benefit (to the extent that the benefit has a *taxable component*).

There are a number of factors that influence the amount of tax payable and the net benefit that will be paid to an adult child.

If your benefit includes a large *taxable component*, an adult child who is a *non tax-dependant* will generally pay tax on this component. However, there is the potential of an *anti-detriment payment* being available, which can largely offset the tax payable on the benefit. The size of an *anti-detriment payment* is typically directly in proportion to the size of the *taxable component* of the death benefit.

Of course, there are generally no guarantees that your fund will be able to provide an *anti-detriment payment* upon your death because it can depend on the nature of the fund and the fund's tax position around the time of your death.

The tax components of your benefit will depend on the type of contribution strategy you had in place while your benefits were accumulating in the fund. For instance, *non-concessional contributions* will effectively increase the *tax free component* of a super entitlement. *Concessional contributions*, along with any investment income added to your account will effectively increase the *taxable component*.

Your adviser may be able to give you more information about possible contribution strategies and how these may impact the tax components of death benefits which become payable to your adult children (and other *non tax-dependants*).

Alternatively, if you're retired and you want to leave your super to your adult children, you may consider giving some or all of your benefits to your children before your death if you can afford to do so. This is because if you are aged 60 or more when you withdraw your super benefits, they will be tax free. Whether or not such a strategy is suitable for you will depend on whether you can afford to give away your benefits and it will need to be weighed up against other considerations, including social security implications. Before undertaking a strategy like this, it's very important to speak to your financial adviser.

Topping up your super with life insurance

If you have a dependent spouse or children, or debts (such as a mortgage), your accumulated super benefits alone may not be enough to ensure your family's well-being after your death. Many superannuation funds offer insurance as an ancillary benefit to members. Topping up your super death benefits with life insurance can be an efficient, tax-effective and inexpensive way to ensure your beneficiaries will be looked after.

The level of cover you need depends on how much super you have accumulated and how much more you might need to cover your debts, income needs of your dependants and expenses such as funeral costs. If you have a large mortgage and young children, you may need a relatively high level of life insurance cover.

As you get older and nearer to retirement, you are likely to experience a lessening of financial responsibilities. Your super balance is likely to be higher, you may have paid off your mortgage and your children may no longer be financially dependent. Therefore, you may not need the same level of life insurance cover that you did when you were younger, or you may no longer need insurance cover at all.

As your circumstances and priorities change, it's important to review your level of life insurance. Your adviser can help you at each step to work out what your insurance needs are, taking into account the level of death benefit you are targeting.

Example 4: Topping up your super with life insurance

Quentin, aged 36, and his partner Rochelle, aged 33, have two children; Sally aged 3 and Tim aged 4 months. Quentin is working full-time and Rochelle has taken a break from work to bring up their children. Quentin and Rochelle have just bought a new home and have a mortgage of $500,000, and approximately $10,000 of credit card and other debt.

Quentin and Rochelle both have superannuation with funds that allow them to make non-lapsing nominations, including child pension nominations.

Quentin and Rochelle's adviser calculates that if Quentin were to die, his family would need approximately $1.7 million in order to pay off the mortgage and credit card debts, cover funeral costs and generate pension income of $15,000 each per year (indexed) for Sally and Tim (until age 25) and $40,000 per year (indexed) for Rochelle until she reaches age 65.

His current superannuation balance is $500,000.

Approximate capital amount needed for pensions[2]	Rochelle	$650,000
	Sally	$200,000
	Tim	$215,000
Mortgage & other debts		$510,000
Funeral costs		$5,000
Education expenses		$120,000
Total capital requirement		**$1,700,000**
Current super account balance		**$500,000**
Top-up cover required		**$1,200,000**

Quentin and Rochelle's adviser suggests that Quentin take out $1.2 million of life insurance cover through his super fund and make non-lapsing nominations directing the trustee to pay some of his death benefits to Sally and Tim as child pensions ($200,000 for Sally and $215,000 for Tim), and the remainder to Rochelle.

Their adviser also suggests that these nominations are taken into account in the drafting of Quentin's will.

Quentin follows his adviser's suggestions and his life insurance cover is approved. If anything were to happen to Quentin, he can be assured that his family will be looked after. Rochelle will be able to choose to receive part of her benefit as a lump sum (to pay off the mortgage and other immediate expenses), and part as a pension. Each of his children and Rochelle will receive a 15% rebate on their assessable pension income.

[2] Based on earnings rate of 7.5% p.a. net of fees and 3% annual indexation of pension payments.

Example 4 (continued):

Ten years on…
Quentin and Rochelle are now working as principals in their own consulting business. Their adviser raises the issue of how the family would manage if anything were to happen to Rochelle. It becomes clear that Rochelle now requires the same level of insurance cover as Quentin.

Quentin and Rochelle have also recently upgraded their house and now have an even bigger mortgage. On their adviser's suggestion, they take out life cover or $1.5 million each. Rochelle also makes a non-lapsing nomination to Quentin and child pension nominations to Sally and Tim.

Another ten years on…
Quentin (now aged 56) and Rochelle (aged 53) have almost paid off their mortgage and now that their children are older, they are not facing the same expenses that they were previously. Their children (now aged 23 and 20) have left home and are working full-time. Quentin and Rochelle each have enough in their super to pay the remainder of the mortgage and other anticipated expenses if either of them were to die. Their adviser suggests that they may no longer need the same level of life insurance cover.

Now that their children are adults, they no longer qualify as *tax dependants* and so it makes more sense for Rochelle and Quentin to review their non-lapsing nominations once more. Their adviser suggests that they nominate each other to receive the balance of their accounts on death. He also suggests that they review their wills once more to take account of the new nominations.

Taking an integrated approach between your super and your will

It is very important to take an integrated approach between your super estate plan and your will. Even though super receives different treatment to other assets on death, it should not be considered in isolation from the rest of your estate plan.

It can be important to think about the tax consequences of leaving your super benefits to certain beneficiaries. For example, if you nominate an adult child, they may pay tax on the benefit. However, if you nominate your spouse or child under 18, they may qualify to receive the death benefit tax free, or at lower tax rates. If you have some beneficiaries who are dependants for tax purposes and others who are not, there may be tax advantages in ensuring your super benefits are paid to dependants, leaving other non-super assets to other beneficiaries.

You may also wish to use your super benefits to provide for your beneficiaries using a combination of lump sum payments, pensions and testamentary trusts. The combination you choose to use will depend on a number of factors including the classes of beneficiaries (whether dependants or not), the ages of your beneficiaries and their income and capital needs after your death. This can only be achieved by integrating your superannuation with your broader estate plan (through your will) and is likely to require co-operation between your financial adviser and solicitor.

Even if your estate plan is relatively straightforward, it's a good idea to ensure that your will takes into account any death benefit nominations you have made and that as your nominations are updated, so too is your will. This will ensure that your intentions are absolutely clear.

Glossary

Accumulation phase is a term used to describe the period when your superannuation benefits are accumulating in the fund. This is the period of time when you are likely to be working and contributing to your super.

Anti-detriment payment is an additional amount that may be paid on top of a lump sum superannuation death benefit. An anti-detriment payment, if payable, will increase the lump sum to an amount that would have been payable had no tax been applied to contributions or investment income of the fund. An anti-detriment payment may be made only when a death benefit is paid to a spouse, former spouse or child (either directly or via the estate).

Interdependency relationship exists between two people if they have a close personal relationship, they live together, one or each of them provides the other with financial support, and one or each of them provides the other with domestic support and personal care. If a person is in an interdependency relationship with another, then that person is considered to be a dependant for the purposes of paying and taxing superannuation death benefits.

Legal personal representative means:

- an executor or administrator of an estate of a person who has died;
- a trustee of an estate of a person who is under a legal disability; or
- a person who holds a general power of attorney that was granted by another person.

Lump sum Reasonable Benefit Limit (RBL) was a lifetime limit on the amount of superannuation benefits you could receive at concessional tax rates. An individual's benefits were assessed against the lump sum RBL unless they invested more than half of their benefits in a complying income stream (in which case may have qualified for assessment against the higher pension RBL). From 1 July 2007, RBLs no longer apply.

Non-assessable non-exempt income is income that is excluded from assessable income. It is a class of income that is ignored for the purposes of working out your taxable income or loss. A key advantage of non-assessable non-exempt income is that it is treated as if it was never received for tax purposes. For example, non-assessable non-exempt income will not be taken into account for determining your eligibility for the Senior Australians Tax Offset or most other tax offsets.

Non-concessional contributions are generally contributions that are not tax deductible. They are typically personal contributions for which you do not claim a tax deduction or contributions that are made for a spouse. These contributions are not taxed when they are made. Non-concessional contributions are also subject to an annual contribution limit which is known as the non-concessional contributions cap.

Pension Reasonable Benefit Limit (RBL) was a lifetime limit on the amount of superannuation benefits you could receive at concessional tax rates. An individual's benefits were assessed against the higher pension RBL if more than half of their benefits were invested in a complying income stream. From 1 July 2007, RBLs no longer apply.

Pre-July 1983 service means the part of your *service period* that occurred before 1 July 1983. The service period is usually the period starting when you first began accruing superannuation benefits.

Reasonable benefit limits – see *lump sum reasonable benefit limit* and *pension reasonable benefit limit*.

Reversionary beneficiary is someone who will continue to receive your pension payments after you die. The pension does not stop, payments simply 'revert' to another person. A reversionary beneficiary is usually nominated when you first commence a pension. Only certain beneficiaries (such as a spouse) are eligible to receive a death benefit in the form of a pension so it's important to keep these in mind when you are making a reversionary beneficiary nomination.

Self managed superannuation fund is a fund that, in general terms, meets the following requirements:

- it has less than five members;
- each member of the fund is a trustee and each trustee is a fund member;
- if the trustee of the fund is a body corporate each director of the body corporate is a member of the fund;
- no member of the fund is an employee of another member of the fund, unless they are related; and
- no trustee of the fund receives any remuneration for their services as trustee.

Service period in relation to a superannuation lump sum, is usually the period of time since you first began accruing superannuation benefits. The service period is relevant in calculating the increased *tax free component* applicable to a disability superannuation benefit and in calculating an *untaxed element* on a death benefit that includes life insurance proceeds (where premiums for the life insurance were claimed as a tax deduction).

SIS dependant in relation to superannuation death benefits is:

- your spouse (including a de facto);
- your child (of any age);

- someone with whom you have an *interdependency relationship*; or
- someone who is a dependant of yours within the ordinary meaning of that term, such as a person who depends on you financially.

Under superannuation law, the trustee is required to cash a member's superannuation benefits as soon as practicable after their death to one or more of the member's SIS dependants or to their *legal personal representative*.

Tax dependant in relation to superannuation death benefits is:

- your spouse (including a de facto);
- your former spouse (if any);
- child under the age of 18;
- someone with whom you have an *interdependency relationship*; or
- someone who is a dependant of yours within the ordinary meaning of that term, such as a person who depends on you financially.

If the deceased died in the line of duty as either a member of the defense force or a police officer, beneficiaries of the death benefit who are not tax dependants will be treated as tax dependants. Death benefits paid to tax dependants receive greater tax concessions compared to benefits paid to *tax non-dependants*. For example, a death benefit lump sum paid to a tax dependant is tax free.

Tax free component is the component of a superannuation entitlement (or benefit) that represents contributions that were not taxed when received by the fund (generally *non-concessional contributions*).

Tax non-dependant in relation to superannuation death benefits, refers to a beneficiary who is not a *tax dependant*.

Taxable component is the value of your superannuation entitlement (or benefit) less the *tax free component* of your entitlement (or benefit).

Taxed element is the part of the *taxable component* of a superannuation benefit representing amounts that have previously been taxed in the fund.

Taxed superannuation fund is a fund that pays tax on assessable contributions and investment income while your benefits are accumulating.

Untaxed element is the part of the *taxable component* of a superannuation benefit representing amounts that have not previously been taxed in the fund. For instance, if you die and have life insurance proceeds paid into your account, your death benefit may include an untaxed element which broadly reflects the fact that no contributions or earnings tax has been applied to life insurance premiums.

Untaxed superannuation fund is one that does not pay tax on contributions or investment income. This can occur because the fund is 'unfunded', where no employer contributions have been made for a member until the member is ready to retire.

If you have any questions or require more information, we recommend you speak to your financial adviser or contact Macquarie:

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