MLC TechConnect

Guide to superannuation death benefits

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1 November 2024

Guide to superannuation death benefits

This guide outlines the rules relating to superannuation death benefits, including who can receive a death benefit and the payment options available to different beneficiaries.

Introduction

A super death benefit is a payment made upon the death of a super member. Generally, the benefit can be paid to one or more of the deceased's dependants and/or to their legal personal representative (LPR). For many clients, their super not only represents a substantial part of their total wealth, it can also help ensure their family and certain other beneficiaries are looked after in the event of death.

The options and rules applying to the payment of death benefits from a super fund can be complicated. It is important to consider possible payment of a death benefit, so super money (including any insured amounts) is paid to the intended beneficiaries in the event of death.

The choices facing clients with larger super balances can be more complex. For example, the transfer balance cap (TBC) limits the amount supporting a retirement phase income stream such as a death benefit pension or account-based pension (ABP).

In this guide, we explain the key technical issues, eligibility requirements, payment options and advice opportunities to understand when considering super death benefits.

Who can receive a super death benefit?

A super death benefit can only be paid to a SIS dependant[1] of the deceased or to the member's LPR[2]. Super does not automatically form part of a deceased estate. However, a member can direct their benefit to their estate by nominating their LPR as the recipient of any death benefit.

There are two definitions of dependant that are relevant for super death benefit purposes. The SIS or super definition determines who can be paid a death benefit and the tax definition determines the taxation of the death benefit.

In simple terms, a super death benefit can only be paid to a SIS dependant, which includes a:

- spouse
- child of any age
- financial dependant
- a person in an interdependency relationship with the deceased, and
- LPR of the deceased.

When a death benefit is directed to an estate (ie LPR), the benefit is distributed according the member's Will. Superannuation proceeds *may* form part of an estate where:

- a valid binding nomination is made in favour of the estate
- the trust deed or fund rules requires payment to an estate in some circumstances (eg no valid binding nomination is in place), or
- the trustee exercises discretion to pay the death benefit to the estate (such as in the absence of a valid binding nomination, when a nomination is non-binding or if the deceased has no SIS dependants).

[1] SISA s10

[2] An exception to this rule applies under SISR 6.22(3) where the deceased has no SIS dependants. A super trustee is permitted to make a payment to an individual who is not a SIS dependant where reasonable enquiries are made, and the trustee cannot find SIS dependants or an LPR.

Some SIS dependants also have the option to receive the death benefit as a pension (refer to Death benefit income streams on page 12.[3]

There are some differences in the definition of a dependant for SIS and tax purposes, which are listed in Table 1 below.

Table 1 – SIS and Tax dependants

Dependant	SIS	Tax[4]
Spouse	Yes	Yes
Former spouse	No	Yes
Child under age 18	Yes	Yes
Child aged 18 or over	Yes	No*
Financial dependant (including adult child)	Yes	Yes
Interdependency relationship (including adult child)	Yes	Yes
Individual who receives a super lump sum because the deceased died in the line of duty as a member of the defence force, Australian Federal Police, state or territory police force or as a protective service officer.	No	Yes

* Unless financially dependent or interdependent.

Spouse

A ‘spouse’ is a person:

- to whom another person is legally married, or
- of the same or opposite sex who is registered as the spouse under State or Territory legislation, or
- of the same or opposite sex who lives with the person on a genuine domestic basis in a relationship as a couple. It will be determined on the circumstances of each case. There is no minimum timeframe that applies.

Former spouses are dependants for tax purposes but not for super purposes. Consequently, a former spouse can receive a super death benefit via an estate, however, a super trustee cannot pay the benefit directly to the former spouse unless the former spouse falls into another SIS dependant category (eg financial dependant) or the trustee cannot find any SIS dependants or LPR.

Child

A ‘child’ includes:

- a biological child
- a child of a spouse
- a stepchild
- an adopted child, or
- a child as defined in the Family Law Act.

It also includes children of a de facto spouse.

[3] SISR 6.21

[4] ITAA97 s302-195

A dependant for tax purposes does not include a child aged 18 or over unless they meet the financial dependant or interdependency definitions.

The term ‘stepchild’ traditionally refers to a child from a previous relationship being brought into a new relationship by one of their biological parents. In these circumstances, the stepchild is a child of the non-biological parent only for as long as the relationship lasts. Therefore, either legal divorce, separation or death of the biological parent ends the parent/stepchild relationship with the non-biological parent[5].

A death benefit nomination made by the non-biological parent in favour of a step-child may be valid after the end of the natural parent/non-biological parent relationship breakdown if the step-child becomes an adopted child, or is financially dependant or in an interdependency relationship with the non-biological parent at their time of death. Otherwise, the non-biological parent can direct their death benefit to their estate and cater for the former stepchild via their Will.

Financial dependant

The term financial dependant is not expressly defined in super or tax legislation but has been considered in the Courts. The key principle from these decisions is that it is not the value of payments received from the client that establishes dependency but the degree of dependency on that payment. This includes the extent the person relies on the financial support provided by another person to meet basic living expenses.

Cases have found financial dependency on payments as small as $20 per week. However, other circumstances, such as where grandparents have paid school fees of their grandchildren, have not established financial dependency. This has been because parents have incurred the liability to pay fees and the payment has been more discretionary in nature than providing for an essential element of life, such as food or shelter. Each circumstance must be considered on its own merits.

It is possible for a person to be deemed a financial dependent under SIS by a super trustee, however, under the same circumstances the ATO has determined no dependency. The view of the ATO is strict, for tax purposes, as a substantial degree of dependency is required.

Interdependency relationship

A person may be in an interdependency relationship[6] if two people:

- have a close personal relationship, and
- they live together, and
- one or each of them provides the other person with financial support, and
- one or each of them provides the other with domestic support and personal care.

If two people satisfy the close personal relationship requirement but cannot satisfy the other requirements, they can still satisfy the interdependency relationship if:

- either or both of them suffer from a physical, intellectual or psychiatric disability, or
- they are temporarily living apart (eg overseas or in gaol).

[5] ATO ID 2011/77
[6] SISA s10A

Trustees consider the following factors when determining if an interdependency relationship[7] exists:

- the circumstances of the relationship including (where relevant):
  - duration of relationship
  - whether or not a sexual relationship exists
  - ownership, use and acquisition of property
  - degree of mutual commitment to a shared life
  - care and support of children
  - reputation and public aspects of the relationship
  - degree of emotional support
  - extent to which the relationship is one of mere convenience
  - any evidence suggesting that the parties intend the relationship to be permanent
- a statutory declaration signed by one of the persons to the effect that the person is or was in an interdependency relationship with the other person.

Not all the listed circumstances must be satisfied for an interdependency relationship to exist. Each factor is given the appropriate weighting depending on the circumstances. Two people do NOT have an interdependency relationship where domestic support and personal care is provided:

- under an employment contract or a contract for services, or
- on behalf of another person or organisation such as a Government agency, a body corporate or a benevolent or charitable organisation.

Generally, it is not likely that children have an interdependency relationship with their parents, but it is possible. ATO ID 2014/22 determined a child and parent were in an interdependency relationship where the child (over 18) had given up work to care for the terminally ill parent and received no financial support from anyone, other than the parent, during that time.

Where a trustee makes a direct payment to an individual, the trustee is responsible for deciding whether an interdependency relationship exists between two people. Check with the super fund what evidence is required. Where the trustee pays a death benefit to the estate, the legal personal representative is responsible for making this decision. If a client is unsure of whether they have interdependency relationship with a potential beneficiary, a prudent approach may be to nominate the LPR for that beneficiary's share of the benefit and update the Will accordingly.

Death benefit nominations

A death benefit nomination can be reversionary for a pension and binding or non-binding for all super interests. Reversionary and binding nominations are only valid at the time of death if the nominated person is eligible to receive the benefit. A member is not required by law to nominate a beneficiary.

When assessing which type of nomination is appropriate, you should consider each client's specific circumstances, including their need for flexibility and other factors such as grandfathering of an ABP for social security purposes and the ability to amend the type of nomination without having to restart the income stream. Certain funds may offer an option to add and remove reversionary nominations without having to cease and restart an existing pension.

For more information, please refer to our **Super beneficiary nominations: options, opportunities and obstacles** article.

[7] SISR 1.04AAAA

Death benefits and social security

Clients must notify Centrelink/DVA within 14 days of a change of circumstances, including the death of a spouse. If a member of a couple dies, a reversionary beneficiary begins to be entitled to payments from the income stream from the date they become entitled to it based on the provider's rules (eg providing a death certificate). The income stream is assessed for social security purposes when they become entitled to the income stream, which may be a different day from date of death. In all other cases, a super death benefit should not be assessed against the surviving partner until the time the trustee decides to pay or commences to pay the death benefit to that person. Practically, this is either at the time the trustee:

- has made a decision to pay a death benefit lump sum to the beneficiary, or
- verifies the beneficiary is entitled to a death benefit pension.

The same rules apply for any other beneficiary of a super death benefit, who also receives a payment or benefit from Centrelink or DVA. Re-directing one's interest in a deceased estate or interest in a super fund will generally trigger the gifting and deprivation provisions.

If a super death benefit is paid to the estate, Centrelink **generally accepts that it may take up to 12 months** for an estate to be administered. However, if a person is able to receive their entitlement at an earlier time, it is at this point that Centrelink/DVA must be notified and re-assess the person's entitlement to benefits.

Compulsory cashing of death benefits

Death is a compulsory cashing event[8] where the death benefit must be paid as soon as practicable after the member dies. The death benefit must be paid as a:

- single lump sum, or
- an interim lump sum and a final lump sum, or
- death benefit income stream to an eligible beneficiary[9] , or
- a combination of lump sum and income stream.

Subject to a fund's governing rules, a lump sum death benefit can be made as cash or as an in-specie payment. An in-specie payment is made using the fund's assets (eg listed shares) instead of money. Death benefit pension payments can only be paid in cash.

Death benefit lump sums

Directly to beneficiary

Superannuation law allows for all SIS dependent beneficiaries to receive a death benefit lump sum. If the deceased has a valid binding nomination, trustees can make lump sum payments directly to beneficiaries.

If a non-binding nomination, an invalid nomination, or no nomination is listed, the rules of the fund determine how the death benefit is paid. Some trustees:

- Exercise their discretion and decide which SIS dependants receive payments. The trustee may also decide to pay to the estate.
- Other trustees may make automatic payment to the deceased member's estate (ie no trustee discretion applies).

Therefore, it is important to understand the rules of individual funds.

Payment to the estate or legal personal representative

Where the super death benefit is paid to the LPR it is distributed according to the Will (or under the intestacy rules if applicable).

[8] SISR 6.21(1)
[9] SISR 6.21(2A)

When a super benefit is paid to the estate, it becomes an 'estate asset' and should the estate be challenged, it may form part of the asset base subject to challenge. This may include any life insurance proceeds from any policies held within the fund.

If the client intends to establish a testamentary trust, it is necessary for the super death benefit to be paid to the estate. The beneficiaries of the testamentary trust would normally be people in the family bloodline, such as parents, children and grandchildren. However, for reasons outlined later, care needs to be taken when deciding who are to be beneficiaries of a testamentary trust to which super proceeds have been directed, as unfavourable tax consequences may be triggered.

To increase tax effectiveness, a testamentary trust comprising super money should be limited to tax dependants such as any spouse or young or disabled children.[10]

Death benefit income streams

Beneficiaries[11] eligible to receive a death benefit as a pension are limited to a:

- spouse
- child under 18 years of age
- child aged 18 to less than 25 who is financially dependent
- disabled child
- financial dependant (other than a child), and
- a person in an interdependency relationship with the deceased (other than a child).

The TBC[12] may restrict how much of a death benefit can be used to commence a death benefit pension and, in some cases, result in an amount being forced out of the super environment.

Where a beneficiary elects to receive a pension (ie a non-reversionary pension) the pension is treated as a new pension. In this situation, the minimum pension payment required for that financial year is determined by the beneficiary's age at commencement date (and every 1 July thereafter) in line with their age and minimum pension payment factors[13]. In the year of commencement, the minimum amount is pro-rated based on the number of days remaining in the year.

For a non-reversionary pension, any pension payments received by the deceased in the year of their death do not count towards meeting the minimum pension standards for the new pension paid to the beneficiary.

Where a reversionary nomination exists, a pension that was payable to the deceased at the time of death can continue to be paid automatically to the reversionary beneficiary (assuming the nomination is valid).

A reversionary pension is a continuation of the original pension and may allow faster processing of a death benefit claim. It also means that a new pension does not commence. This does not necessarily prohibit the pension from being commuted in part or in full (subject to the rules of the fund and type of pension).

As a reversionary pension continues following death, the minimum payment required in the financial year in which death occurred is the amount which applied to the deceased. On the following 1 July, the beneficiary's age (and not the deceased's) is used to determine the minimum pension payment required for that financial year.

Death benefits received as an income stream are still identified as death benefits.

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[10] Specialist legal and tax advice should be obtained in this instance to ensure that the Will provides adequate provision for the establishment of a trust and to ensure the structure of any trust provides tax effective outcomes for the beneficiaries.

[11] SISR 6.21.

[12] A TBC between $1.6m and $1.9m applies (24/25), depending on the client's situation.

[13] SISR Schedule 7

Rollover death benefits

Death benefits paid may be rolled over to another fund for immediate cashing.[14] That is, a death benefit can be rolled over to another fund for immediate commencement of a death benefit pension in the new fund. Rolled over amounts cannot be retained in the accumulation phase.

Rolling over death benefits may be appropriate where the beneficiary is to receive death benefits from multiple funds and wishes to consolidate the death benefits to a single death benefit pension, or where the fund from which the death benefit is payable does not have an appropriate pension option. Whether a client should have one or multiple death benefit pensions depends on their circumstances (eg consider the tax components of various benefits along with the desire for ease of management.

Death benefits cannot be consolidated with a beneficiary's own member benefits (nor be held in accumulation phase). If the beneficiary has their own account-based pension, they must consider the appropriateness of running multiple death pensions given that they will need to keep the death benefit separate at all times.

Taxation of super death benefits

The taxation of super death benefits depends on:

- whether the payment is taken as a lump sum or an income stream
- whether the beneficiary is a dependant for tax purposes
- if taken as a death benefit pension, the age of the deceased at death and the beneficiary's age at payment, and
- the underlying tax components of the interest.

A death benefit is always treated and taxed as a death benefit, regardless of when a payment or commutation of a death benefit pension is made to a beneficiary from the fund.

Determining tax components of the interest

A death benefit may comprise a taxable component and a tax-free component. Any death benefit payment made reflects the proportions of the tax components of the deceased member's interest. The tax components of the death benefit reflect:

- the components of the interest at the time of a lump sum payment paid from accumulation phase
- in the case of a reversionary pension, the components of the pension fixed at the time the deceased initially commenced their pension, or
- in the case where the deceased held a non-reversionary pension, the tax components of that interest, which commences to be paid as a death benefit pension.

As a result of this proportioning requirement, in the case where there are multiple beneficiaries of the same interest, the death benefit paid to each beneficiary comprises tax components in the same proportion as the overall interest at the relevant time.

Taxation of death benefit lump sums

Only the taxable component of a death benefit is potentially subject to tax. The **tax free** component of a death benefit lump sum is never taxed regardless of who is the beneficiary. The taxable component is generally made up of amounts that have been taxed in the super fund, known as the **taxed element**. The taxable component may also include an amount that has not been taxed in the fund. This is known as the **untaxed element** and can arise in certain public sector schemes.

An untaxed element may also arise in respect of some death benefit lump sums comprising of at least part insurance proceeds where the trustee claimed a deduction[15] on premiums. The untaxed element is not simply the insured amount but is rather an amount derived from a formula in the act[16].

[14] SISR 6.21 (3).

[15] A fund (generally restricted to eligible SMSFs) that DOES NOT claim a tax deduction for insurance premiums paid in the financial year that a death or disability amount is paid can claim a deduction for future liability, where the person ceases gainful employment (ITAA 1997 S295.470).

[16] ITAA97 S307-290.

Calculating an untaxed element

Untaxed element	= taxable component – taxed element
Taxed element	= (lump sum super death benefit × service days / (service days + days to retirement)) – tax-free component
Days to retirement	= number of days between date of death and the deceased's last retirement date (generally age 65)
Service days	= number of days from the member's eligible service date to date of death.

Eligible service date is the earlier of:

- the date the member joined the fund, or
- if a rollover amount is received, the date with an earlier eligible service period, or
- if the member's employment commenced before they joined the fund, their employment commencement date where the employer contributed to their fund.

The untaxed element broadly reflects the future service period of the death benefit. An earlier service date effectively increases the taxed element and decreases the untaxed element. An earlier service date may be achieved by rolling funds with an earlier start date into a super fund with insurance.

Lump sums paid directly to tax dependants

If a death benefit is paid as a lump sum from a taxed super fund, no tax is payable on any amounts received by a tax dependant. This includes payments from both the tax-free and taxable components.

Lump sums paid directly to non-tax dependants

If a death benefit is paid as a lump sum to a non-tax dependant (commonly a financially independent adult child), the tax payable on the various components is summarised below.

Table 2 – Tax payable by non-tax dependants on lump sums

Component	Maximum rate of tax payable (excluding Medicare levy)
Tax free	Nil
Taxable	Taxed element: 15%* Untaxed element: 30%*

* Medicare levy/surcharge may also apply.

If the death benefit is paid from the super fund directly to a non-tax dependant, the fund must withhold tax at the lump sum tax rate plus Medicare levy. The taxable component is added to the person's assessable income, taxed at up to the maximum rate (either 15% or 30% plus Medicare levy) and a credit is applied for the tax withheld by the super fund trustee.

The additional income may cause the person to lose some Government benefits or concessions that are based on assessable or taxable income, as income increases (even though maximum rates of tax applies). Examples include Family Tax Benefit, Government co-contributions or the Low Income Tax Offset.

Lump sums paid to the estate

A super fund does not withhold any tax when a death benefit is paid as a lump sum to the estate. Instead, the lump sum is taxed in the hands of the executor of the estate in the same way as it would have been if paid directly to the person(s) intended to benefit from the superannuation death benefit. However, in this case, Medicare levy is not payable. Therefore, executors must withhold the appropriate amount of tax prior to distributing it to beneficiaries who are not dependants for tax purposes and remit this amount to the ATO. Beneficiaries of an estate do not pay tax personally on any amount of the death benefit and the payment is not included in their income tax return.

Super proceeds that flow into a testamentary trust

If the death benefit flows from the estate into a testamentary trust, the tax withheld by the estate on the death benefit depends on whether or not all the beneficiaries of the trust are dependants for tax purposes.

If **all** beneficiaries are tax dependants, the amount is not taxed, as would have been the case if paid to them by the fund directly, or if the executor had directed the proceeds to the beneficiary in their individual capacity.

If **any** of the beneficiaries of the trust are non-tax dependants, the executor is required to withhold tax on the entire taxable component as if the benefit was paid to a non-tax dependant. An exception may exist if the executor can determine the amount of the death benefit that flows via the testamentary trust for the benefit of a tax dependant.

Advice tip

Specialist legal advice should be provided in relation to the Will and upon the death of the individual to ensure that the Will contains the required provisions to bring support to any testamentary trust arrangement and, that upon establishment, the trust deed will sufficiently support this arrangement.

Taxation of death benefit income streams

The table below summarises the tax payable on tax components based on the age of the recipient (at the date of payment) and the deceased (at the date of death).

Table 3 – Tax payable on pension payments from death benefit income streams

Age of deceased at death / beneficiary at time of payment	Component	Tax treatment
Either aged 60 or over	Tax Free	Tax-free
	Taxable – taxed element	Tax-free
	Taxable – untaxed element	Taxed at marginal rate less 10% pension tax offset (no tax offset for income exceeding $118,750 in 2024/25)
Both under age 60	Tax Free	Tax-free
	Taxable – taxed element	Taxed at marginal rate less 15% pension tax offset (when recipient turns 60, becomes tax-free)
	Taxable – untaxed element	Taxed at marginal rate (when recipient turns 60, a 10% pension tax offset applies for income up to $118,750 in 2024/25

Commutations withdrawn from a death benefit pension are always treated as a superannuation lump sum death benefit for tax purposes and are received tax-free.

Pensions to minor children

Minor children who receive a pension are taxed as adults (ie it is excepted income and child penalty tax rates do not apply). A death benefit pension paid to a child (who is not disabled) of a deceased member can only be continued until the child reaches age 25.[17] At this age, the pension must be commuted and any residual capital is paid as a tax-free lump sum.[18] However, a pension being paid to a disabled child can continue indefinitely. Partial withdrawals are not permitted from child pensions[19]. It is important to note different product providers may have different interpretations of the legislation. Therefore, it is worthwhile confirming with the product provider whether partial withdrawals are permissible.

When does a pension cease?

If the deceased member was in receipt of an income stream and there was no auto-reversionary death benefit nomination in place at the time of their death, for tax purposes (ie 0% tax on earnings within the fund) the pension continues to the extent that a death benefit is paid as soon as practicable.[20]

This means that if assets need to be sold down to pay a death benefit, the fund remains entitled to claim exempt current pension income until this time. Consequently, any capital gain realised is not subject to capital gains tax to the extent that the asset supported the pension interest. Any investment earnings from date of death until the death benefit is paid are recorded in the same proportion of tax-free and taxable component as at pension commencement.[21]

Transfer balance cap

A death benefit received as a pension must be a superannuation income stream that is in retirement phase. The beneficiary has their own TBC and does not inherit the deceased's TBC. The value of a death benefit pension (excluding children) is assessable against the beneficiary's personal TBC[22] and counts toward their transfer balance account (TBA). A client's personal TBC is calculated with reference to:

- whether they have previously had a retirement phase income stream
- the general TBC at the time the individual first commenced to have a TBA, plus
- any proportional indexation of the cap.

The amount of a death benefit that can be taken as a death benefit pension may be limited by:

- the amount of the death benefit itself (which may include any life insurance proceeds payable), as well as
- any additional amounts the beneficiary has previously used to commence their own superannuation retirement phase pensions.

Before implementing death benefit strategies, advisers need to consider the:

- value of the beneficiary's personal TBC
- value of the beneficiary's TBA
- available TBC space
- timing for when the credit of the death benefit pension applies in the beneficiary's TBA
- requirement, if any, to commute an amount or the entire balance of the beneficiary's existing retirement phase pension to avoid accruing an excess transfer balance, and
- fact that a death benefit cannot be rolled into accumulation phase, however, can be rolled over to another super fund to be immediately received as a new death benefit pension (including the timing of debits and credits associated with the transaction).

[17] This applies to death benefit income streams commenced on or after 1 July 2007.
[18] ITAA97 s303-5.
[19] SIS reg 6.21(2A)
[20] TR 2013/5: Income tax: when a superannuation income stream commences and ceases.
[21] ITAR 307-125.02
[22] A TBC between $1.6m and $1.9m applies (2024/25), depending on the client's situation.

The ability of a child to receive a death benefit pension may be limited further by the operation of the modified TBC rules that apply to child beneficiaries. The following sections explain the advice considerations and options available for implementing death benefit strategies.

Advice tip

Advisers need to consider whether commencing a death benefit pension and triggering a TBA is appropriate or whether cashing the death benefit and investing the proceeds outside of super is a better alternative.

For example, if a beneficiary receives a death benefit pension when they are younger, say in their 20s or 30s, is it appropriate for them to use all or part of their TBC at that time? In this scenario, the beneficiary may fully or partially exhaust their available TBC as well as the death benefit (retirement phase) pension before they reach their own retirement.

A death benefit income stream also reduces the beneficiary's ability to access indexed increases to the TBC at a later stage. For more discussion on the TBC rules please refer to our article **Guide to the transfer balance cap.**

Non-reversionary pension

A credit of a non-reversionary pension[23] occurs on the beneficiary's TBA at the time the trustee commences payment of a death benefit pension. The value of the credit includes any investment earnings or losses accrued between the date of death and the commencement of the death benefit pension.

Example 1: TBA credit applied on commencing a non-reversionary death benefit pension

Zoey died on 1 October 2024 with an ABP valued at $250,000. Zoey had previously made a valid binding death benefit nomination to her husband Zac. Zac elects to take the death benefit as a pension which commences for Zac on 1 January 2025 when the account balance increased through investment growth to $280,000.

The credit to Zac's TBA is equal to the commencement value of $280,000.

Now assume that Zac also had his own ABP which commenced in July 2018 with an amount of $1.6m[24] . If Zac wishes to take Zoey's death benefit as an income stream and retain all funds in the super/pension environment, he would need to ensure that a partial commutation of $280,000 is made from his own ABP to create a debit against his TBA before the death benefit is commenced on 1 January 2025. The partial commutation is rolled back to accumulation

[23] This includes a death benefit pension commenced from the deceased accumulation interest or an income stream paid to the deceased which did not have a valid reversionary nomination.

[24] The general TBC in 2018/19 was $1.6 m. This means Zac will not receive any benefit from any increase in the general TBC has he has no unused proportion.

Reversionary pension

It is only when an automatic reversionary nomination exists that the credit to the TBA occurs 12 months from the date of death of the member, based on the value of the pension at date of death.

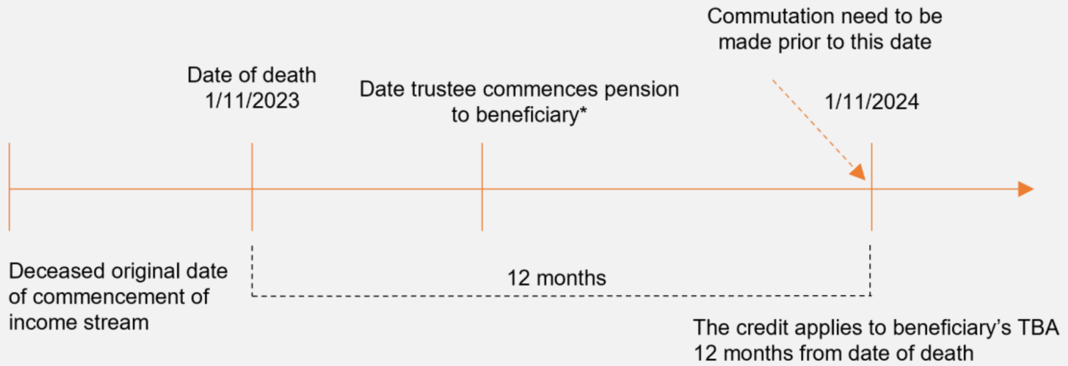
This may afford the beneficiary (ordinarily the surviving spouse) additional time to seek advice to ensure that an excess transfer balance amount does not occur. During this period, it is possible for the surviving spouse to hold more than their personal TBC in retirement phase. Exempt current pension income can be claimed on both their existing pension and their reversionary pension.

Example 2: TBA credit applied on automatically receiving a reversionary death benefit pension

William died on 1 November 2023 holding an ABP with a balance of $1m at the time of death. The pension reverted to his wife Wendy. During the next 12 months the pension balance grew to $1.1m through investment earnings.

On 1 November 2024, Wendy's TBA received a credit of $1m in respect of the reversionary pension, being the value of the pension at date of death. The value of the pension at 1 November 2024 ($1.1m) does not impact Wendy's TBA.

Now assume Wendy has her own ABP which commenced with $1.6m in August 2018. She wishes to retain as much as possible in the super/pension environment so will need to commute $1m of her own ABP and move this back to the accumulation phase. The commutation must occur before 1 November 2024 (ie 12 months after the date of death) to avoid breaching her personal TBC.



* Although reversionary pension is continuation of original pension, the trustee must still ensure that nomination is valid, receive necessary paperwork prior to commence paying to beneficiary

As the assessment of the death benefit pension does not count towards Wendy's TBA until 12 months from the date of the death, she can continue to receive both income streams during this time. The value of the reversionary pension is based at the date of death and ignores any subsequent positive or negative growth.

Example 3: Beneficiary has an account based pension

Wayne and Jane are married. Both commenced account based pensions in January 2018 with $1.6m each and made reversionary nominations to each other. Wayne passed away on 1 August 2023, when his pension was valued at $1.6m. After the trustee completed the death benefit process, the reversionary commenced in favour of Jane. On 1 August 2024, a credit of $1.6m applies to Jane's TBA, which is the value of the pension on the day Wayne died.

On 25 July 2024 (just before 12 months from the date of death), Jane fully commutes her existing ABP. At this time:

- Jane's own pension balance has decreased to $1.5m, and
- the value of the reversionary death benefit is $1.55m.

Jane's transfer balance cap is $1.6m (she used her TBC in full in 2017/18, therefore her TBC is not indexed).

The following table illustrates her TBA credits and debits.

Date and Event	Credit	Debit	TBA	Explanation
1/1/2018 Jane commenced an account based pension	$1.6m	-	$1.6m	Credit is equal to commencement value
1/8/2023 Wayne died and $1.6m pension reverted to Jane	-	-	$1.6m	Pension reverted to Jane, however, no credit applies to her TBA at that time as pension is reversionary
25/7/2024 Jane fully commutes her own account based pension back to accumulation phase	-	$1.5m	$100,000	Debit value equals amount commuted. Jane's TBA is $100,000 (credit of $1.6m less debit of $1.5m)
1/8/2024 $1.6m credit applied for reversionary death benefit	$1.6m	-	$1.7m	The credit applied is equal the pension value at date of death, despite the fact the current pension value has decreased by $50,000 to $1.55m. Jane has exceeded her TBC by $100,000.

Outcome: As Jane has fully commuted her own pension, she will need to commute an additional $100,000 lump sum from the reversionary pension. For every day she has a transfer balance excess, she will need to commute an additional amount which will reflect notional earnings on the amount in excess. She will also be liable for excess transfer balance tax.

If Wayne had nominated Jane as a binding death benefit nomination (as opposed to reversionary) a similar outcome could also arise. If Jane commenced a new death benefit pension either prior to or after she fully commuted her own pension, an excess transfer balance could still occur if the combined commencement values (credits) applied for her own pension and the new death benefit pension less the commuted pension value (debit) exceeds her personal TBC of $1.6m.

Child death benefit pensions

Death benefit pensions payable to eligible child beneficiaries are also subject to the TBC rules. The amount of the TBC applied to a child death benefit pension is referred to as a TBC increment. However, this does not impact the child's individual TBA for their own retirement savings in the future.

Transfer balance cap increment

A separate TBC increment applies to each death benefit pension the child receives from a parent. A child may have multiple cap increments which are added to determine the maximum amount a child may transfer to pension phase. The cap increment is calculated based on whether the:

- child pension commenced prior to 1 July 2017 or after
- deceased parent had a TBA or not
- child is the sole beneficiary of the death benefit or one of many, and
- deceased parent had an excess transfer balance at the time of death.

A child's total cap includes the sum of cap increments in respect of the death of one parent, the death of both parents, and/or their own member pension (from permanent incapacity proceeds or from structured settlement contributions).[25]

Child death benefit pensions must be fully commuted once they turn 25 (unless disabled) with any remaining capital paid as a tax-free lump sum.[26] At this point, the modified TBC is extinguished. If the death benefit pension balance is exhausted prior to 25, the modified TBC ceases at the earlier time.

If the child is disabled, the modified TBC continues beyond 25 until the balance of the pension is extinguished. This ensures that the child's own personal TBC is preserved and not eroded by the receipt of a death benefit pension.

Advice tip

An amount of a death benefit payable to a child may be forced out of the superannuation environment based on the structure (accumulation or pension phase) or value of their deceased parent's super benefit as explained below.

It is important for advisers to communicate with clients the responsibilities that a guardian will have when acting as trustee for a child that has received an amount from a super death benefit or through a deceased estate. The trustee will need to invest the proceeds and distribute the capital and income to the child in accordance with their wishes, any fund rules and legislative requirements.

Mindful of the TBC limitations, it is important for advisers to discuss with clients:

- how much of a super benefit should be directed to SIS dependants directly?
- how much of a super benefit should be directed to their estate?
- should provisions for a testamentary trust be included or updated in the client's Will?

Also remember the child will have control of the ABP from age 18 and can make decisions regarding access to capital from that age. From age 25, the child death benefit pension must generally cease, and any remaining capital paid out. Given these elements, clients should consider whether they wish for children to have access to capital from age 18 and, if not, explore alternative estate planning strategies, such as a testamentary trust.

[25] A debit applies to TBA equal to the amount of the contribution made under a structured settlement.
[26] ITAA97 s303-5

Child death benefit pensions commence prior to 1 July 2017

The child TBC increment is $1.6m for child death benefit pensions that commenced prior to 1 July 2017. This was equal to the general TBC on that date. Any excess above $1.6m was required to be cashed out of superannuation before 30 June 2017. Scenarios for child death benefit pensions that commenced since 1 July 2017 are covered below.

Deceased did not have a transfer balance account

A deceased parent does not have a TBA at the time of their death if they never commenced a retirement phase income stream (excludes transition to retirement income streams). The child's TBC increment is:

- the general TBC ($1.9m in 2024/25), if the child is the sole beneficiary, or
- the child's proportionate share of the deceased's superannuation interests multiplied by the general TBC, if the child is not the sole beneficiary.

That is the **child TBC cap increment** = child's % share of accumulation interest x general TBC

Example 4: No transfer balance account, benefit wholly from accumulation

Sole beneficiary

In December 2024, Mary (44) passes away leaving her super accumulation interest of $2.1m to her daughter Rita (16) as the sole beneficiary. As Rita is the sole beneficiary her TBC increment is the general TBC of $1.9m.

Rita can commence a death benefit pension up to $1.9m and take $200,000 (the amount that exceeds the cap increment) as a lump sum death benefit.

Multiple beneficiaries

If Rita was instead entitled to 50% of Mary's accumulation interest ($1,050,000), with the other 50% payable to her father Tom, her cap increment would be calculated as follows:

50% x general TBC = $950,000.

Rita could therefore commence a pension with $950,000 of her $1,050,000 entitlement and would need to take the remaining $100,000 as a lump sum death benefit.

Deceased with a transfer balance account

If a deceased parent had a TBA, a death benefit to a child beneficiary may either be paid:

- wholly from a pension interest
- wholly from an accumulation interest, or
- partially from accumulation and pension interests.

A child's TBC increment is determined by their percentage share of the deceased parent's retirement phase income streams. This means once a parent has a TBA, generally any death benefit pension commenced from the parent's accumulation interest will result in an excess transfer balance cap.

Example 5: Parent had TBC, benefit wholly from pension

Alex passes away in October 2024. At the time of his death he has an ABP valued at $4m. He does not have an excess transfer balance amount. Paula (daughter age 14) and her brother Liam (son age 11) are both beneficiaries of Alex's pension interest in equal proportions (ie 50% each). Each would have a cap increment calculated as follows:

= 50% x $4m = $2m.

Child pension commencement values are limited by their percentage share of their parent's total retirement phase balances. This means a child death benefit pension can commence with a balance greater than the general TBC at that time.

If Alex had instead passed away without a TBA and the interest was paid wholly from accumulation, each child would only have a cap increment of $950,000 (as per example 4). This means the maximum amount that they could hold in death benefit pensions would be $950,000 each. The remaining $1,050,000m each (from the initial $2m each) would be paid as a lump sum death benefit to each of the children.

TBC increment where both parents die

Where both parents die, the child's TBC increment is the sum of amounts worked out in relation to each parent. This involves:

- calculating their available cap increment for each parent
- adding the available cap increments together, and
- adding to that any personal TBC increment the child has in respect of their own member pension (from permanent incapacity proceeds or from structured settlement contributions).

Options for amounts exceeding TBC

Investing amounts exceeding TBC

If a client exceeds their TBC upon receiving a death benefit pension (or 12 months after death for a reversionary pension), they must commute an amount from retirement phase. As death benefits cannot be rolled back to accumulation phase, clients may wish to consider commuting the excess amount from their own member pension(s) as these amounts can be rolled back to accumulation. In this situation, clients who wish to maximise the amount held within the super environment based on their overall circumstances can do so.

Alternatively, an amount can be withdrawn from the superannuation system. If taken from the death benefit, it is tax free (as a person who is eligible to receive a death benefit pension is also a tax dependant). If the beneficiary is less than age 60 or has an untaxed fund, withdrawals from the beneficiary's own interest may have tax implications. However, maintaining the excess amount in the accumulation phase of super may not always provide an optimal outcome.

Investing an amount outside of super for people with low assessable income levels may result in that client paying less tax. Assessable income from assets held in super accumulation phase is taxed up to a maximum rate of 15%. The availability of the tax-free threshold and various tax offsets means the non-super option could provider a lower effective tax rate for certain clients.

When determining whether to invest an amount inside or outside of super, you should consider the client's overall financial circumstances and objectives. A client may wish, regardless of the tax outcome, to hold as much of their investments as possible inside super for estate planning purposes. A binding death benefit nomination allows a death benefit to be paid direct to a specific super dependant. In this situation, the invested amount in super will generally not be subject to challenge in their deceased estate[27].

[27] Exception is in NSW under notional estate rules. Care should be taken to review nominations on ongoing basis to ensure valid.

Withdraw death benefit and recontribute to super

A dependant beneficiary may wish to withdraw all or part of a death benefit and recontribute to super (the recontribution strategy) if:

- they are eligible to make non-concessional contributions (NCCs)
- they wish to convert taxable component to tax-free component to reduce any future tax payable for non-dependent beneficiaries
- tax on their personal assessable income exceeds the superannuation tax rate of 15% and therefore they are subject to a lower tax rate by investing inside super, or
- an amount held in accumulation phase is not assessable for social security entitlements if the person is under age 67 and they wish to apply for or are receiving Disability Support Pension or JobSeeker Payment.

The recontribution strategy may have to be in the current financial year if their total super balance at next 30 June will prohibit them from making future NCCs.