

Fast death tax - The Tax Office changes its view

by Matthew Burgess, Director, View Legal

So called 'fast death' tax arises where superannuation benefits that could otherwise be withdrawn tax free by the member of a superannuation fund during their lifetime, remain in the fund at the date of death of the member and are then subject to tax on the distribution from the fund.

The tax detriment so branded due to the fact that if a member dies of (say) a heart attack the tax will be triggered, whereas where a terminally ill member is given (say) 4 months to live they will likely have sufficient time to withdraw all benefits. Arguably an unnecessarily capricious piece of superannuation legislation, introduced by amendments a few years ago.

There are generally three potential pathways to manage this form of death tax, namely:

1. ensure the funds are withdrawn prior to death, while the member has capacity;
2. implement a complementary enduring power of attorney, allowing an attorney to withdraw funds if a member loses capacity, ensuring the withdrawal is completed before the donor's death;
3. the member could sign a direction as to future withdrawal, with the effective date defined as being (say) one day prior to their death. In relation to this approach, if a complementary enduring power of attorney is in place, then the attorney could sign such a direction.

The first two approaches appear to be accepted by the Tax Office, subject only to any anti avoidance arguments. This said, given the concessionary tax regime of superannuation is forgone - potentially for an extended period - these approaches are perhaps unlikely to be seen as offensive.

Historically the third approach has also been approved in a number of Private Rulings issued by the Tax Office.

The approach was generally centred around a member signing as part of their estate planning arrangements a direction as to future withdrawal, with the effective date of the withdrawal set as being (say) 1 day before the date of the death of the member.

The robustness of the approach is now however also subject to the Tax Office publication 'Paying superannuation death benefits', released in February 2023 as QC 45254.

In this publication the Tax Office states:

1. If a member requests an amount to be paid from their fund before they die, but dies before they receive it, it may be a member benefit in some 'limited' cases. The outcome in this regard is said to be 'determined by the facts and circumstances surrounding the payment'.
2. The relevant facts and circumstances listed by the Tax Office are set out as including:
 - (a) terms of the request from the member;

(b) terms of the trust deed and any other governing rules;

(c) knowledge of the trustee at the time the payment is made (including whether the trustee is aware that the member has died);

(d) the entity that the payment is being paid to (eg the member's personal account or an account in the name of the member's legal personal representative);

(e) circumstances and timing of the payment;

(f) whether the payment is made because of and in line with the request made by the member.

Critically in the examples provided in QC 45254 the Tax Office draws particular distinctions on the following items, apparently making them key factors in determining whether a payment after death is a member benefit or a death benefit; namely whether:

(A) the trustee was aware that the member was deceased at the time of the payment (with the trustee being unaware supporting a conclusion that the payment is a member benefit);

(B) the payment was made to an account in the name of the member, or in the name of the member's legal personal representative (with payment to the member's account supporting a conclusion that the payment is a member benefit).

As flagged in the examples, this seems to indicate that the Tax Office believes SMSFs will be unlikely to substantiate payment of a member (as opposed to death) benefit post death (given the trustee is almost certain to be aware that the member has died) as compared to an APRA fund where the trustee may be unaware of the member's death at the date of payment.

Furthermore, unless the purported member benefit payment is supported by the trust deed and implementation documentation and made to the bank account of a member, any payment following a member's death is likely to be treated by the Tax Office as a death benefit.

