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The new rules quietly creating a death tax as government eyes great wealth transfer

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Officially, Australia does not have a death tax.

But two separate tax developments in recent months have confirmed that death taxes are due to become a lucrative new area of tax revenue.

In each case, the tax is a technical "tweak" to an existing situation, but combined, these new tax developments confirm a trend.

The most contentious of the changes is found in the new super tax.

Put simply, in the first version of the new super tax, it did not matter at what time of the year an investor died; the estate was not liable for the new tax. But in the updated version now before parliament, it matters significantly.

Financial adviser Liam Shorte says it will create a precedent for death taxes.

"The death tax development introduced by the new super tax does not affect a large portion of the population, but the precedent is the issue, and steadily the principle of death tax becomes acceptable within the tax system," Shorte says.

As Shorte explained in a recent episode of The Australian's The Money Puzzle podcast, once the new super tax is up and running, the tax will be worked out based on the higher of your balance at the start of the year and your balance at the end of the year.

"And so, if a person dies, say, in January, they'll have had six months' tax due," Shorte says.

"For somebody trying to handle a deceased estate, there is a desire to get the money out to the grieving family. But now they'll have to wait until the 30th of June and look at what the earnings were for the full year."

Consequently, as well as there being potential for extra tax to be paid, there's the very real prospect that dispersing funds from estates would be delayed significantly.

As tax lawyers and financial advisers get to grips with the new super tax rules, the Australian Taxation Office caught the wider market by surprise in late January with a fresh ruling on what Matthew Burgess at View Legal calls "the family home death tax".

Again, this is another tweak in the system that brings death taxes back into the mainstream, even though such taxes are supposed to have been eliminated decades ago.

"If a family home passes to a testamentary trust, the ATO is now saying capital gains tax will be triggered on the ultimate sale – essentially creating a death tax," Burgess says.

"Testamentary trusts are a standard modern estate planning structure many families use to manage and protect wealth."

A testamentary trust is established through a will and comes into effect after the death of the person who made the will.

“Testamentary trusts are particularly important in situations such as blended families, where grandparents wish to provide for grandchildren or where there are ‘at-risk’ individuals: for example, mental or physical incapacity, substance abuse, or gambling addictions,” Burgess says.

Constant tweaks to the tax system, where death or inheritance tax developments imply higher costs, mean the potential for substantial tax revenue increases in the future.

The looming transfer of intergenerational wealth is a useful target. It is estimated that across Australia, $3.5 trillion worth of assets will be inherited in the coming decades.

Industry statistics show that 70 per cent of people born in the 1960s “expect to inherit”, but the number rises to 80 per cent for those born in the 1980s.

In fact, millions of Australians are already in the frame for the death tax through superannuation.

With super savings the biggest asset for most people outside of the family home, the effective 17 per cent tax imposed on most superannuation inherited by adult children has become a mainstream issue. Increasingly, superannuation investors are embarking on so-called recontribution strategies in an effort to reduce this tax.

Two new tax changes being branded as death taxes within a matter of months spell it out: death taxes are back on the government’s agenda