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## Did You Know?

"Effective from 21st September 2007, Age Pension gets a six-monthly increase of 2.4% bringing the 12 month increase to 5.0%. Age Pensioners are now benefiting significantly from the government's decision a few years ago to use the greater of CPI and Average Wages inflation when calculating 6 monthly increases".

Source: [www.findem.com.au](http://www.findem.com.au)

## Superannuation Death Benefits – paid to a non-dependant

On 1<sup>st</sup> July 2007 the new Australian superannuation rules came into operation.

In this article we look at the taxation of superannuation death benefits when they are paid to a beneficiary who is not "dependant".

The Tax Act defines a dependant as the spouse, former spouse, child under the age of age of 18, any other person who is financial dependant on the super fund member, or a person with whom the deceased member has an interdependency relationship with.

Let's look at a simple example of Stan. Stan is aged 84 and is receiving superannuation benefits by way of a regular income stream paid from his superannuation. Sadly Stan's wife, Jean passed away 3 years ago. He has 2 daughters, Elizabeth and Judy, both of who are independent of Stan and have their own families with adult children.

When Stan finally passes on, it is his wish that any remaining balance in his superannuation account will be shared equally by his two daughters.

As Stan's daughters are not financially dependent on him, there may be taxation consequences when Stan's superannuation passes on to Elizabeth and Judy.

The superannuation reforms that came into effect from 1<sup>st</sup> July 2007 allow a person to withdraw their superannuation benefits (from a taxed superannuation source) tax free once they reach age 60 and have met a condition of release (e.g. retired). In Stan's case, if he were to withdraw his superannuation benefits as a lump sum he would not pay any tax on those benefits. Where a superannuation death benefit passes to a dependant, that benefit is also paid tax free. However, a superannuation death benefit that passes to a non-dependant may well be taxed at a rate of up to 15% plus Medicare Levy. If the superannuation benefits include proceeds of life insurance, the tax rate could be as high as 30%, plus Medicare. From a tax planning perspective, it would be advantageous for Stan to be able to

withdraw his savings from the superannuation system prior to his death.

So what are Stan's options?

Firstly, he could withdraw his superannuation benefits now as a lump sum and simply invest the money outside of the superannuation system to generate a regular income stream to meet his living needs. The disadvantage of this option is that Stan receives from investment earnings outside of superannuation which may not be as tax efficient as receiving a tax free income stream from superannuation.

As a second option, Stan could continue to draw his superannuation income stream but make a series of lump sum withdrawals tax free during his twilight years. Once again, this would introduce the potential problems outlined in the first option.



As most people enter a stage of declining health prior to passing away, Stan could conceivably leave his savings in the superannuation system until close to his demise. As health declines during the later stages of life, Stan may not have the capacity to make the necessary decision to draw down his superannuation entitlements whilst still living. To overcome this, Stan should consider having his daughters (or other trusted person) appointed under an Enduring Power of Attorney. The advantage of appointing an attorney is that they can act in the place of Stan. Should his health decline and the end of life becomes imminent, the attorney could arrange to withdraw Stan's superannuation.

getting you from **a** to **b**

As he is still living at the time of withdrawal, the superannuation benefits would be paid out tax free. This way, Stan continues to receive the benefit of tax free income from his superannuation fund for as long as possible, and then withdraws his lump sum at the most effective time. If Stan had \$1,000,000 in super (all taxed component), withdrawing the benefit prior to his death would save his daughters \$165,000 in tax.

An important aspect of the third strategy is that the person holding the enduring power of attorney must know who to contact in the event of the person they are acting for going into a stage of declining health.

Note: If Stan was a member of an untaxed superannuation scheme, such as a State or Commonwealth Government super fund, the taxation treatment of his benefits may differ from that described in this article.

Source: Peter Kelly – Professional Investment Services

## Changes to Income Protection Insurance



For many years it has been an established practice for many people to hold their Life, Total and Permanent Disablement (TPD), and Income Protection Insurance (also referred to as *Salary Continuance* or *Disability Income insurance*) through superannuation. The effect of this strategy is that the superannuation fund arranges the insurance on the life of the member. This can help with managing personal cash flow as it is the super fund that pays the premiums. Premiums will generally be tax deductible to the super fund. However, when it comes to Income Protection insurance, there were historical reasons as to why holding this inside super may not have been the most effective strategy. Income Protection Insurance is designed to replace income in the event of the insured suffering from an illness or disability. The insured selects

the term that benefits are to be paid for. For example, a benefit period may be provided for a maximum of (say) 2 years, or to a specified age (such as to age 60 or 65).



In the past, the Australian Taxation Office only allowed a tax deduction for Income Protection Insurance premiums to the extent that the premium related to a 2 year benefit period. That is to say, if a person held Income Protection Insurance inside super that provided benefits to (say) age 65, only a portion of the premiums would be tax deductible. With this in mind, many super funds used to limit the level of Income Protection Insurance cover that they offered through super to a 2 year benefit period.

Earlier this year the Australian Taxation Office announced they were removing the year benefit period limitation on deductibility of Income Protection Insurance premiums.

A super fund may now claim a tax deduction for Income Protection Insurance premiums irrespective of the length of the benefit period. It is therefore an opportune time for people who hold their Income Protection Insurance through their superannuation fund to review the terms, conditions, and benefit periods applicable to their cover.

Of course, where a person holds Income Protection Insurance in their own name (that i.e. outside of super), the premiums will generally also be tax deductible at the personal level. With this in mind, appropriate structuring of the ownership of your Income Protection Insurance (inside or outside super) becomes critically important.

Source: Peter Kelly – Professional Investment Services



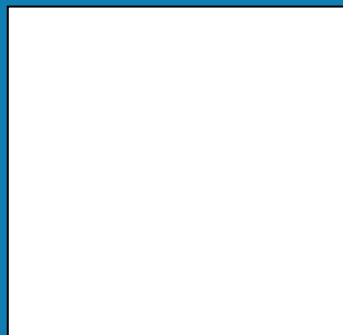
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