PCG 2017/6 - Superannuation reform: commutation of a death benefit income stream before 1 July 2017

Superannuation reform: commutation of a death benefit income stream before 1 July 2017

Relying on this Guideline

This Practical Compliance Guideline sets out a practical administrative approach to assist self-managed superannuation funds comply with the *Superannuation Industry (Supervision) Regulations 1994*. Provided you follow this guideline in good faith, the Commissioner will administer the regulation in accordance with this approach.

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What this Guideline is about

1. An individual may choose to commute a superannuation income stream that is a superannuation death benefit (death benefit income stream). If the individual was the spouse of the deceased member and certain other criteria are met the individual may choose to roll-over the commuted amount to or within a self-managed superannuation fund (SMSF) for immediate cashing.

2. This Guideline outlines the circumstances in which the ATO will not apply compliance resources to review whether a SMSF has satisfied the requirement to cash out a death benefit in this situation where the roll-over occurred prior to 1 July 2017.

3. All references are to the *Income Tax Assessment Act 1997* (ITAA 1997), unless otherwise stated.

Application

4. This Guideline will have effect both before and after its issue.

Who this Guideline applies to

5. This Guideline applies to an SMSF that receives a superannuation lump sum resulting from the commutation[1] of a death benefit income stream where the commutation occurred in circumstances described in paragraph 16 of this Guideline.

Background

6. When a member of a superannuation fund dies, a superannuation provider is required to cash the deceased member's remaining superannuation interests to their beneficiaries or their legal personal representative as soon as practicable.[2] The payment of the superannuation interest after the member's death is called a superannuation death benefit.[3]

7. For dependant beneficiaries of the deceased, superannuation death benefits can be cashed:

- as a superannuation lump sum (either in a single or an interim and final lump sum) that is paid out of the superannuation system[4]
- as death benefit income streams that are retained in the superannuation system[5], or
- a combination of the two.

8. Where the superannuation provider cashes a deceased member's superannuation interest to a dependant beneficiary as a death benefit income stream, the compulsory cashing requirement is met as long as the superannuation income stream continues to be paid.

9. A superannuation provider will not comply with the compulsory cashing requirement if it allows the deceased member's superannuation interest to remain in the accumulation phase after a time when it became practicable to cash the deceased member's superannuation interest.

10. The regulatory provisions allow superannuation providers one limited exception to the requirement to cash the deceased member's superannuation interest. This is where the deceased member's superannuation is rolled over to another superannuation fund as soon as practicable for immediate cashing by the other superannuation provider.[6]

11. The Commissioner has become aware that industry participants have inferred that subsection 307-5(3) provides a mechanism for the spouse of a deceased member to roll over a death benefit income stream and retain the amounts as their own superannuation interest without the need to immediately cash-out that benefit. We understand this inference resulted from issuing public guidance[7] without explicitly clarifying the cashing requirements and led to an industry practice adopting this position.

12. The Commissioner's view is that the roll-over by a spouse of a deceased member's death benefit income stream does not change a superannuation provider's regulatory requirement to cash the deceased member's superannuation interest as soon as

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[1] The Commissioner has previously set out a practical compliance guideline concerning commutations made before 1 July 2017 in order to comply with the transfer balance cap in PCG 2017/5 *Superannuation reform: commutation requests made before 1 July 2017 to avoid exceeding the $1.6 million transfer balance cap*.
[2] See regulation 6.21 of the *Superannuation Industry (Supervision) Regulations 1994* (SISR).
[3] Subsections 307-5(1) and (4).
[4] Paragraph 6.21(2)(a) of the SISR.
[5] Paragraph 6.21(2)(b) of the SISR.
[6] Subregulation 6.21(3) of the SISR.
[7] Taxation Determination TD 2013/13 *Income tax: is a payment by a complying superannuation fund (first fund) to another complying superannuation fund of a superannuation lump sum arising from the full commutation of a superannuation income stream paid to a person as a beneficiary of a deceased member of the first fund, a 'roll-over superannuation benefit' for the purpose of section 306-10 of the Income Tax Assessment Act 1997?*

practicable. This means that the superannuation provider that has received the rolled over death benefit must immediately cash the deceased member's superannuation interest in the form stated in paragraph 7 of this Guideline.

13. However, the Commissioner acknowledges that the industry practice that has developed means that a number of death benefit income streams have been commuted, rolled over and treated as the spouse's own superannuation interest. This may have resulted in the amounts commuted from the death benefit income stream becoming mixed with the spouse's other superannuation interests and/or remaining in accumulation phase.

14. In recognition of the inference drawn resulting in the industry practice and the significant practical difficulties for superannuation providers that have adopted this position to trace, value and then cash superannuation death benefits if they were now to try and apply the Commissioner's position, the Commissioner will adopt the compliance approach outlined in this Guideline.

15. This approach only applies in respect of superannuation death benefits that have been rolled over before 1 July 2017.

Our compliance approach

16. The Commissioner will not apply compliance resources to review whether a SMSF has complied with the compulsory cashing requirements relating to a death benefit as set out in regulation 6.21 of the SISR provided that:

- the member of the SMSF was the spouse of the deceased on the deceased's date of death; and
- the commutation and roll-over of the death benefit income stream is made before 1 July 2017[8]; and
- the superannuation lump sum paid from the commutation is a member benefit for income tax purposes because it meets the requirement of subsection 307-5(3).

Example 1

17. *Henry dies on 1 January 2015. At the time of Henry's death he was in receipt of a pension from the Jackson Superannuation Fund valued at $1,000,000. This pension reverts to Henry's spouse, Kate.*

18. *Kate has her own accumulation phase interest ($500,000) in the Kate SMSF and wishes to consolidate all of her superannuation entitlements. Therefore, on 1 August 2015 Kate instructs the Jackson Superannuation Fund to commute the reversionary superannuation income stream in full and roll the amount over to her accumulation phase interest in the Kate SMSF.*

19. *The superannuation lump sum resulting from the commutation meets the conditions of subsection 307-5(3).*

20. *The Commissioner will not apply compliance resources to review whether or not the Kate SMSF has complied with the compulsory cashing requirements related to the death benefit.*

[8] The requirement that the commutation take place before 1 July 2017 is based on the current application of the repeal of subsection 307-5(3). The exposure draft of Treasury Laws Amendment (2017 Measures No.2) Bill 2017 proposes that the repeal of that subsection applies on the day after that Bill is introduced into the House of Representatives.

Example 2

21. *Justin and Edwina are members of SMSF A. On 1 October 2014 Justin commenced a pension with SMSF A valued at $2,500,000. The rules of the pension do not provide that it may revert to another person on Justin's death. Justin dies on 1 January 2015.*

22. *On 15 June 2015, Justin's remaining superannuation interest is paid to Edwina, his spouse, as a death benefit income stream from SMSF A. Edwina also has her own accumulation interest with SMSF A.*

23. *The value of the superannuation interest that supports the death benefit income stream just before 1 July 2017 is estimated to be $2,300,000.*

24. *If Edwina does nothing, her transfer balance on 1 July 2017 will likely be $2,300,000 and exceed her transfer balance cap ($1,600,000).*

25. *To prevent an excess transfer balance, Edwina partially commutes the death benefit income stream by $700,000 (the amount that will exceed her transfer balance cap) before the 1 July 2017.*

26. *The superannuation lump sum resulting from the commutation meets the conditions of subsection 307-5(3).*

27. *Edwina instructs SMSF A to roll over the commuted amount to her accumulation phase interest within the SMSF A.*

28. *The Commissioner will not apply compliance resources to review whether or not SMSF A has complied with the compulsory cashing requirements related to the death benefit.*

Commissioner of Taxation
22 May 2017

References

ATOlaw topic(s)	Superannuation ~~ Income tax - individuals (superannuation) ~~ Other
Legislative references	ITAA 1997 ITAA 1997 307-5(1) ITAA 1997 307-5(3) ITAA 1997 307-5(4) SISR SISR 6.21 SISR 6.21(2)(a) SISR 6.21(2)(b) SISR 6.21(3)
Related Rulings/Determinations	TD 2013/13
Other references	PCG 2017/5