

Précis Paper

Binding Death Benefit Nomination tips and traps

A discussion about superannuation estate planning, including binding death benefit nominations, the ramifications of them, the potential for them to be displaced and the importance of proper estate planning to avoid issues that can result from binding death benefit nominations.

Discussion Includes

- Self-managed superfunds
- Control of the superfund after death
- Laws governing superannuation
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- Binding Death Nomination and Mutual Wills Deeds
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Binding Death Benefit Nomination tips and traps

In this edition of BenchTV, Dung Lam (Special Counsel, Coleman Greig Lawyers, Sydney) and Elizabeth Burnheim (Senior Associate, Coleman Greig Lawyers, Sydney) discuss superannuation estate planning, including binding death benefit nominations, the ramifications of them, the potential for them to be displaced and the importance of proper estate planning to avoid issues that can result from binding death benefit nominations.

Self-managed superfunds

1. When estate planning, it is important to understand the family matrix of the client. This helps to understand the options that are available to the client, taking into account the family matrix and what the client's ultimate goal is as a binding death nomination is not the only way to deal with superannuation in estate planning. It is also perhaps not the best option.
2. If there is a self-managed superfund and someone wants to ensure that the trustee pays the superannuation a certain direction, it may be better to hard wire the proposed gift of superannuation death benefits in the superfund's trust deed. This takes out the need for a binding death benefit nomination and also takes out the potential challenges concerning whether the binding death benefit nomination is valid.
3. On the other end of the spectrum where there are no foreseen challenges in the family matrix, perhaps a client desires flexibility and in that case it may be best to have no hardwired direction in the superfund's trust deed or in a binding death benefit nomination. Rather the focus would be to ensure that control of the superfund is left to the correct persons on death.
4. If a binding death nomination is valid and binding and a person loses capacity, there is no

way of changing it or removing it. That is one key danger of making a binding death benefit nomination.

5. With recent cases examining binding death nominations, it is clear that how control of the superfund passes on death is exceedingly important and it is not enough to just rely on a binding death nomination. That is, it is imperative to know who is going to be in control of the superfund once the client has died. This is because even if the binding death benefit nomination is valid the remaining trustee/s of the superfund left after death may choose not to follow it.

5. This was exemplified in the matter of *Wooster v Morris* [2013] VSC 594. In this case, a father wanted his daughters from the first marriage to get the super death benefits and made a binding death nomination to this effect. However, the superfund was a husband and wife fund and once he died, control reverted back to his wife. The wife refused to follow the binding death benefit nomination made by her deceased husband. The daughters incurred significant legal costs in enforcing the binding death benefit nomination against the remaining trustee of the fund (i.e. the wife).

Control of the superfund after death

6. Considering control of the superfund after death is really relevant to self-managed superfunds because where the client is a member of an industry or retail superfund control of the fund is out of their hands.

7. In the context of a self-managed superfund to assess how control passes on the death of a member one must look at who is the current trustee of the superfund and the rules of the fund to find out what the succession of the trustee role is. In particular, it is important to note who has the power to appoint and remove the trustee pursuant to the rules of the fund.

8. Quite commonly a self-managed superfund might have a corporate trustee in place. If this is the case it is necessary to determine who the directors of the corporate trustee are and who holds the shares. A review of the company constitution of the corporate trustee should also be done to consider how directors are appointed to the board of the corporate trustee. As a side note it is also important to decide who the executor of the estate is going to be. If the executor is also a shareholder, they may have the ability to step in and appoint himself as sole director if the deceased was the only member of the fund.

Laws governing superannuation

9. Superannuation law has multiple layers of law. A superfund is actually a trust, governed by trust law. Overlaid on this trust law is Federal superannuation law which outlines certain rules which the trustee of the superfund must comply with if the superfund wishes to access the generous tax concessions available to the complying superannuation funds. Therefore in working with superfunds it is necessary to consider trust law (including the provisions of the trust deed governing the fund) and Federal superannuation law and tax law.

Tax implications of gifting superannuation death benefits

10. Confusingly the superannuation law has a concept of superannuation dependants which is different from the tax concept of a superannuation dependant.

11. Superannuation law (i.e. the *Superannuation Industry (Supervision) Regulations 1994*)

governs who can receive a member's superannuation death benefits on their death. Broadly this covers a spouse, a child, and a person who was either financially dependent on the deceased member at the date of death or a person in an interdependent relationship with the deceased at the date of death.

11. Then there is the tax concept of a dependents which governed by the tax rules. These tax rules determine whether the recipient pays tax on their receipt of a member's superannuation death benefits.

12. The key difference between these two concepts are adult children who are dependents for superannuation purposes but not for tax purposes. As noted above dependents for superannuation purposes.

include spouses, children of all ages, people in an interdependent relationship and are dependent. These are the people who can receive the death benefit.

13. On the tax side of things, people who do not pay tax on super are spouses, minor children, and children under the age of 25 who are studying full time will receive the tax free. Adult children who are financially independent however, have to pay tax on the taxable component of the superannuation death benefit they receive.

Giving a superannuation death benefit to executor

14. The Executor will pay tax depending on where it gets distributed. To the extent that the whole of the superannuation passes through the estate and passes to the spouse, it will be tax free.

15. If it goes to the adult independent child, then the Executor is required to pay tax at 15%. If

the adult child were to receive that superannuation payment directly and it did not go via the estate, the child would have to pay the 15% plus the Medicare levy. Therefore, having it go through the estate even if it goes to the adult child has the potential to have a small tax saving.

16. It is imperative to always look at the rules of the fund because even if the superannuation laws define who can receive superannuation death benefits, the actual rules of the fund may refer to a much narrower class. If the rules of the SMSF do not allow for a binding death nomination a person can organise for them to be updated to include provisions for making such nominations if desired.

17. When one is in a retail or industry fund, they are at mercy to the rules of the fund. Some superfunds do not give members the ability to make a binding death nomination and only a non-binding wish as to how benefits are paid. In this case, the trustee of the superfund ultimately has the discretion to decide who amongst the people who can receive under Superannuation law will receive the death benefits.

Definition of spouse

18. It is imperative to look at what is the definition of spouse under the fund rules and the superannuation law in considering whether a death benefit can actually be paid to a person who you may consider is the deceased member's partner in life.

19. There was a recent case of *Howard v Batistich* [2019] FCA 525 where somebody was considered a 'de-facto spouse' and received a death benefit after dating the deceased for around 4-5 months. They were not living together; however, she was awarded the death benefit as she was considered a 'spouse' under the rules of the superfund (which here was a state based superannuation fund whose rules were legislated under state law). The deceased's parents sought to overturn the decision to gift their son's death benefit to his girlfriend – the parents would have benefited from their son's deceased estate. The case went through the the Superannuation Complaints Tribunal and was ultimately appealed to the Federal Court. The case came down to the definition of 'spouse' under the rules governing the fund and evidence where the girlfriend showed she had text

messages which showed that they were in a loving, committed relationship together.

20. Further, for clients going through a divorce, who are separated it is important for lawyers to advise clients to review and perhaps revise their binding superannuation death benefit nominations. This is because it can take time for a divorce (12 months before the decree nisi) and it

would be unfortunate if a divorcing party died and their death benefit went to their ex-spouse if this was not intended.

Pitfalls of drafting

21. It is recommended that one seek legal advice on making a binding death benefit nomination because the nomination needs to be in accordance with the rules of the superfund and superannuation law.

In the case of *Munro v Munro* [2015] QSC 61 a lawyer who drew up his own binding death nomination. The idea was for the death benefit to go into the lawyer's deceased estate and be gifted under the terms of his will. The problem was the terminology used in the binding death benefit nomination which provided that the death benefit go 'to the trustees of my estate'.

22. The rules of the fund did not define what the 'trustee of the estate' actually meant and the superannuation law does not refer to this term either, rather the superannuation law uses the term 'legal personal representative' which includes the executor of a deceased estate. The binding death benefit nomination was held to be invalid because this incorrect terminology was used.

Stepchildren

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23. The superannuation law defines a 'child' using the common law definition. This raises an issue for step-children. This is because under the common law a step child's relationship with their step parent is severed on the death of their natural parent. For instance this means that whilst the husband and wife are still alive and married together, the children on either side are children of both. They are superannuation dependents for both parents. On the death of the first of the parents, the spouse can receive the death benefit and so can all of the children as they are regarded as dependents of the deceased parent. The step relationship, however, is broken.

24. On the death of the second parent, the children of the first parent to die are no longer superannuation dependents of the second parent to die. The second spouse cannot distribute their super directly to the stepchildren. This poses a problem in happy families where the step-parent wants to gift their superannuation to all of the couple's children (including their step children). Where this is the case, the work around is for the step parent to gift their death benefits to their deceased estate and manage the gifts under the terms of their Will.

Challenging binding death nominations

25. In *Katz v Grossman* [2005] NSWSC 934, a father wanted to give his super equally between a brother and sister. It was sole member fund and the sister was the other trustee for the self-managed fund.

26. He did not make a binding death nomination however he wrote his wishes in his will.

However, the sister took control of the fund and in her own discretion gifted all the money to herself. For a long time *Katz v Grossman* was seen as indicating that the trustee of the superannuation had an absolute discretion to determine who gets a superannuation death benefit, where there is no binding death benefit nomination. The case law now indicates that this position is no longer absolute.

27. The case law now, shows that the typical ways to attack how a death benefit is to be distributed are:

- a. To attack the validity of the binding death nomination
- b. They try to attack the trustee position, that is who controls the superfund and may thus decide who gets the death benefit
- c. Conflicts of interest – i.e. arguing that the trustee has a conflict of interest and so their decision as to who gets the death benefit is invalid at trust law

28. Where there is a surviving spouse, often the surviving spouse is also the executor under the will. Once probate is granted, an executor has a fiduciary obligation to the estate. This can cause conflicts of interest for example in circumstances where it is not in the interest of the surviving spouse to challenge the nomination personally however it is in the estate's best interests to challenge the nomination such that it is gifted to the estate. The surviving spouse has a conflict of interest. It is important to insert a clause in the will to excuse the Executor from a potential conflict in dealing with the superannuation of the will-maker and also authorise them to deal with superannuation, where the executor is the surviving spouse and it is intended that they receive the death benefit.

29. In the case of *McIntosh v McIntosh* [2014] QSC 99 an administrator of the estate was the deceased's mother. The deceased son had lived with his mother for 30 years. She had divorced his father when he was young. The mother made an application for the payment of his death benefits as an interdependent person as they were living together and providing each other with emotional and financial support, and it was paid to her. However, she was also the administrator of his deceased estate. The father came back into the picture realising he could have a share of the son's superannuation death benefit if he could overturn the gift of the superannuation to the mother. He argued

that the payment of the death benefit to the mother was invalid as there was a conflict of interest between her position as administrator of the estate whose role was to maximize deceased estate assets and her receipt of the death benefit. The Court agreed with the father and overturned the gift to the mother.

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30. The case of *Marsella v Wareham (No 2)* [2019] VSC 65 indicates that where there is no binding death benefit nomination, it is not exactly right to say that the trustee of the superfund has an absolute discretion to determine who receives the benefit of a deceased member's death benefits. The trustee's decision making still needs to be in accordance with trust law.

31. In this case, the daughter was the sole the superfund trustee. She appointed her husband as co-trustee with her, and thinking that she had an absolute sole discretion to make the decision as to who can receive the death benefit, made

the decision to pay the death benefit to herself without regard to other potential beneficiaries' claims. The daughter was a child of the first marriage.

32. Her step-father was the applicant in the matter and challenged her decision to gift the death benefits of her mother to herself. The court said that whilst a trustee has a discretion to determine who receives the death benefit on the death of a member where there is no binding death benefit nomination, the trustee must still give due consideration to the potential beneficiaries' claims to the superannuation

death benefit. As the daughter and her husband as trustees had exercised the trustees' discretion to distribute the death benefit to the daughter without a real and genuine consideration of the step-father's claim for the death benefit, the Court overturned their superannuation death benefit decision and removed them as trustees of the fund.

33. Where there is a discretion for the payment of a death benefit, the best way for a trustee to deal with it is by taking an orderly claim staking process. This means undertaking a process where you are identifying the potential beneficiaries, asking them to outline why they should be considered for a receipt of a death benefit distribution, alerting them of the decision, and giving the other prospective beneficiaries the chance to object to the decision.

Binding Death Nomination and Mutual Wills Deeds

34. The concept behind a mutual wills deed is contract law and promissory estoppel which backs it up. It is an agreement between parties (generally spouses) that their Wills will be drafted in a particular way with particular gifts, and that either party will not change their Wills without agreement of the other party. Mutual wills deeds can tighten up binding nominations to ensure superannuation gets paid to certain persons. Mutual wills deeds can also be used for

persons who want flexibility.

35. The mutual wills deed can ensure that the surviving party cannot change their will to gift assets which a couple has built up over their lifetime to parties other than the parties that the couple have decided jointly will benefit from their assets on their deaths. It can be used to protect children of the first marriage from a concern that the surviving spouse may re-partner and change their will and gift joint assets to the new partner.

Reversionary Pension

36. If there is a reversionary pension one needs to look at the rules of the superfund to see how a reversionary pension interplays with a

binding death nomination

37. Generally, most super funds have rules that say if you have a reversionary pension, it

trumps the binding death benefit nomination. If a client has a reversionary pension, it is

important to work out who the reversionary beneficiary is and if the reversionary beneficiary is the person intended to receive the client's death benefit then there may be no need to do a binding death benefit nomination.

38. Reversionary pensions are immediate, upon death the pension automatically goes to the spouse.

Power of Attorney

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39. The case of *Re Narumon Pty Ltd* [2018] QSC 185 looks at whether a person can give an attorney the power to make a binding death nomination in the case where the principal

loses capacity. In this case, there were a number of binding death benefit nominations

which the spouse, who was the attorney at the time purportedly tried to put in place

40. Two of them were merely refreshing ones that had already been in place. Then there were

other fresh new binding death benefit nominations which she purported to put in place using her power of attorney to put

41. The Courts drew the distinction between the Attorney affirming what had already been put

in place and the entirely new nominations. *Narumon* was concerned with Queensland succession law and the Queensland power of attorney legislation. The ability of an attorney to making a binding death benefit nomination varies from state to state. For instance in NSW the Supreme Court case of *G v G* (No. 2) [2020] NSWSC 818 suggests that it may not be possible for an attorney to make a binding death benefit nomination in NSW for a person who has lost capacity.

BIOGRAPHY

Dung Lam

Special Counsel, Coleman Grieg Lawyers, Sydney

Dung Lam currently holds the position of Special Counsel within Coleman Grieg's Taxation Advice team, having joined the firm as part of our 2019 integration with Argyle Lawyers. With extensive experience in Federal taxes including income tax, capital gains tax, GST and State taxes such as stamp duty, land tax and payroll tax, solving complex tax issues comes naturally to Dung.

She also advises clients on self-managed superannuation funds, taxation trusts and tax issues related to estate planning. Her clients include corporates families and their advisors and high net worth individuals. Dung creates tax effective strategies for clients who wish to undertake acquisitions, disposals of assets and businesses, business restructures, domestic and international business.

Elizabeth Burnheim

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With over 6 years' experience, she has a breadth of knowledge and experience in handling complex taxation issues, which often involve assisting high-net worth clients, business owners, trustees and beneficiaries of trusts. Elizabeth advises her clients on their business and investment structures for payroll tax purposes such as de-grouping applications and payroll tax audits. From assisting SMSFs acquire property using limited recourse borrowing strategies, to large payroll tax audits, to amending trust deeds for NSW Surcharge Purchaser Duty, to complex estate planning matters involving inter vivos and testamentary trusts, no day is the same.

Elizabeth often presents at internal and external seminars and various tax discussion groups around Sydney and for The Tax Institute and Legalwise. She has also written multiple articles for the

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