Superannuation and Wills

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1. **INTRODUCTION**

1.1 Superannuation is increasingly becoming a major asset for more and more Australians.

   For retirees, superannuation is often the next largest or only other asset after the main residence due to the tax benefits available for investment income. For younger Australians, automatic group insurance cover in retail and industry superannuation funds means that they often have substantial life insurance (far in excess of their contributions) in superannuation.

   Superannuation is also a significant asset for all those people in between due to a combination of insurance, the effects of superannuation guarantee over the course of their careers and reduced contribution caps forcing people to start planning for retirement earlier in life.

1.2 For all these groups, their superannuation is a major asset that must be dealt with regardless of whether they are preparing a basic will or implementing a complex estate planning strategy.

1.3 Too often, estate planning strategies do not consider how superannuation integrates into the estate plan, or the estate planning and superannuation strategies have not been considered at the same time.

   It is essential in developing any estate planning or superannuation strategy that the other is also considered. A good strategy that builds wealth in superannuation, but does not consider how it will be passed on is flawed as is an estate planning strategy that does not specifically consider the issues inherent in superannuation death benefit planning.

   Preferably, superannuation and estate planning should be considered together. I have seen situations where a client had a great superannuation strategy and a great estate planning strategy, but they had been developed independently. As a result, they did not work together and, when combined, failed to achieve the client’s ends.

1.4 There are many elements that interact together and must be considered and balanced in light of the various strengths and weaknesses when dealing with superannuation death benefits, including:

   (a) the terms of the trust deed, which are paramount, and the applicable trust law;

   (b) the requirements of the *Superannuation Industry (Supervision) Act 1993* and *Regulations 1993* (to be referred to as the *SIS Act* and *SIS Regulations*);

   (c) the tax implications on superannuation death benefits under the *Income Tax Assessment Act 1997* (these issues are not considered in this paper); and

   (d) where there is a trustee company, the terms of the constitution and the application of the *Corporations Act 2001*.

1.5 Also, given superannuation is now such a major asset, it is critical that you include clauses when drafting a client’s Will that appropriately deal with superannuation.

1.6 There are a number of potential traps as well as opportunities presented by superannuation in estate planning, and it is important to be aware of them. This paper aims to provide an overview of some of these traps and opportunities.

2. **SUPERANNUATION IN YOUR WILL – WHAT YOU CAN AND CANNOT DO**

2.1 Superannuation death benefits do not automatically form part of an estate and therefore cannot be primarily dealt with in a Will.

   As a result, it is critical to understand how superannuation death benefits are paid so that an appropriate estate planning strategy can be developed.
Payment of superannuation death benefits

2.2 Death is a compulsory cashing condition – therefore a benefit must be paid from the superannuation fund in some form after the death of a member.

2.3 The SIS Regulations set out how and to whom the superannuation death benefit can be paid, but within that class provides the trustee with an absolute discretion.

Who can receive a superannuation death benefit?

2.4 Under regulation 6.22, the trustee can pay to any ‘dependant’ or to the estate.

‘Dependant’ is defined in section 10 of the SIS Act to include:

(a) the deceased’s spouse;
(b) the deceased’s children;
(c) people who are, at the date of death deceased’s death:
   (i) actually financially-dependant on the deceased; and
   (ii) in an interdependency relationship with the deceased.

2.5 The definition of ‘spouse’ in the SIS Act has been amended by the Same-Sex Relationship (Equal Treatment in Commonwealth Laws – Superannuation) Act 2008 to include people:

(a) in a registered relationship (some states have the ability to formally ‘register’ relationships); and
(b) who, although not legally married, live together on a genuine domestic basis in a relationship as a couple.

This expands the scope of ‘spouse’ and opens it to a wider category of people, particularly same sex couples who were not included in the old definition.

Section 22C of the Acts Interpretation Act 1901 contains a list of factors to consider whether people are in a ‘de facto relationship’ which are similar to those used in the Family Law Act 1975. Although the phrase ‘de facto relationship’ is not used in the SIS Act, these factors could be helpful in deciding whether a couple are ‘spouses’ for the purposes of the SIS Act.

The factors are:

(a) the duration of the relationship;
(b) the nature and extent of the couple’s common residence;
(c) whether a sexual relationship exists;
(d) the degree of financial dependence or interdependence, and any arrangements for financial support between the couple;
(e) the ownership, use and acquisition of the couple’s property;
(f) the degree of mutual commitment to a shared life;
(g) the care and support of children; and
(h) the reputation and public aspects of the relationship.
2.6 The definition of ‘child’ in the SIS Act has also been amended\(^1\) to include:

(a) an adopted child;

(b) a step-child;

(c) an ex-nuptial child;

(d) a child of the person’s spouse; and

(e) a child under the Family Law Act 1975.

This again expands who can be considered a ‘dependant’ for superannuation. For example, if you have a ‘spouse’, then your ‘child’ includes your spouse’s children, which effectively includes your spouse’s step-children.

However, it is important to remember that your spouse’s children will only remain your ‘child’ for superannuation death benefit purposes whilst their parent remains your spouse. If that child’s parent dies first, then that child will not be a ‘child’ for the purposes of the survivor’s superannuation death benefit and therefore the client will only be an eligible beneficiary if they have been formally adopted or are in a financial or interdependency relationship with the survivor. This is a particular issue for blended families.

The inclusion of a person as your ‘child’ is not dependent on the relationship you have with them, so it could dramatically impact on the scope of people who are included in the definition of dependant.

2.7 The ‘interdependency relationship’ is a more recent addition. Two people are in an interdependency relationship if:

(a) they have a close personal relationship;

(b) they live together;

(c) one provides the other with financial support; and

(d) one provides the other with domestic support and personal care (section 10A of the SIS Act).

Examples could include:

(a) same sex couples (although same sex couples will often now be ‘spouses’);

(b) parents and children; and

(c) siblings.

There is an exception to the requirement to ‘live together’ where one or both of the parties to the relationship suffer from a physical, intellectual, psychiatric disability.

**In what form can a superannuation death benefit be paid?**

2.8 Regulation 6.21 permits the trustee of a superannuation fund to pay the death benefit as either a lump sum or a pension. This paper will not explore the issues in relation to the form of the superannuation death benefit payment in detail.

2.9 However, it is important to note that a pension can only be paid where the recipient is a ‘dependant’ of the deceased at the time of death.

\(^1\) Same-Sex Relationship (Equal Treatment in Commonwealth Laws – Superannuation) Act 2008
Also, there are additional restrictions where that person is a ‘child’ of the deceased (see regulation 6.21(2A)).

The importance of the trust deed

2.10 Whilst the SIS Regulations outline the compliance requirements for the payment of death benefits, the trust deed for the superannuation fund is paramount when it comes to paying a superannuation death benefit. It is essential that this is properly considered as part of the estate planning process. In my experience, the trust deed is often less flexible and imposes additional and unnecessary requirements on the payment of a superannuation death benefit.

2.11 That being said, most superannuation trust deeds still afford the trustee a wide discretion to determine how death benefits are paid – although that discretion is subject to the terms of any reversionary pension or binding nomination.

Dealing with superannuation death benefits in a Will

2.12 The superannuation death benefit is not an asset that forms part of the estate and cannot be dealt with under a Will unless the trustee’s discretion is exercised in favour of the estate or the estate is the pre-determined recipient under a binding nomination or by operation of the trust deed.

2.13 Where the superannuation death benefit does become an estate asset, the Will is able to deal with the superannuation death benefit in any manner the testator determines. In particular, there is no limitation on who can receive the superannuation death benefit under a Will and it often forms part of a testamentary trust.

2.14 Although there is no restriction on who can receive the superannuation death benefit under a Will, there can be varying tax consequences depending on who receives the death benefit. The tax treatment of superannuation death benefits is a complex area that is dependent on a number of issues. As a result, it is a topic in itself and is beyond the scope of this paper. However, there are a couple of fundamental taxation concepts that need to be understood:

(a) Firstly, you need to be mindful of whether the beneficiary is a dependant for the purposes of the Income Tax Assessment Act 1997. This is a different definition to the definition of ‘dependant’ for the purposes of the SIS Act.
(b) Secondly, the tax rate that applies will depend on the components that make up the superannuation death benefit. Each superannuation death benefit payment will be made up proportionately of a range of components, including taxable, tax-free and untaxed, depending on how the amount came to be in the superannuation system. Each of these components has a different tax treatment.

In paragraph 6.2, I discuss some clauses that you should consider when drafting a Will to best manage these issues where the superannuation death benefit forms part of the estate.

2.15 It is essential that any well drafted Will deal with superannuation death benefits regardless of whether or not it is intended to form part of the estate for a number of reasons:

(a) The superannuation death benefit may form part of the estate even where this was not the desired outcome. As a result, it is critical that the consequences of the superannuation death benefit being received by the estate are properly thought through and dealt with in the Will.
(b) The superannuation death benefit may be paid to an unintended recipient. Since the trustee of the superannuation fund has a wide discretion, it is possible for it to be used in favour of a person who was not the desired recipient. This can result in a very different outcome to that intended by the testator particularly where the provision left under the Will was made on the assumption of the intended outcome.
For example, it is not unheard of for a trustee to decide, considering your assets, your Will and the needs of your dependants, to pay all of your benefits to a child from a previous marriage, rather than the current spouse.

In both the above situations there are some drafting considerations that should be taken into account to deal with these possibilities (see paragraph 6.2).

2.16 Also, where the testator has a self-managed superannuation fund (SMSF), the control of the SMSF needs to be considered so that the death benefit decision is made by the correct person.

To adequately address the control of an SMSF on the death of the member, the Will, the SMSF trust deed and the trustee company constitution (where applicable) need to work together.

This issue is discussed further in paragraph 7.

3. BINDING DEATH BENEFIT NOMINATIONS – TO THE ESTATE?

3.1 The trustee’s discretion in relation to the payment of superannuation death benefits can be a very powerful tool in ensuring that the superannuation death benefit is dealt with appropriately. This is particularly the case in the SMSF environment, where you have control over the distribution and can use the benefits from superannuation payments very effectively with full knowledge of the facts at the time of making the decision.

3.2 However, there are cases where a lack of certainty and wide flexibility created by the trustee’s discretion can be a serious problem. In these cases, it may be necessary to consider the use of a binding nomination.

3.3 Section 59 of the SIS Act and regulation 6.17A of the SIS Regulations allow the trust deed of a superannuation fund to be structured such that a member can make a nomination that is absolutely binding on the trustee in relation to how their death benefit is to be paid.

However, the provisions in the SIS Act and the SIS Regulations regarding binding nominations only apply to retail and industry superannuation funds and not SMSFs. As a result, there are slightly different considerations for each type of fund.

**Binding nominations and retail/industry superannuation funds**

3.4 The SIS Act and SIS Regulations only allow a superannuation trust deed to contain the provisions enabling binding nominations – they do not themselves give the beneficiary the power to make a nomination that is binding on the trustee. For a member to be able to make a binding nomination, the trust deed for the superannuation fund must be appropriately worded. Therefore, it is essential before making a binding nomination that the trust deed provisions are carefully considered.

3.5 Also, any process specified in the trust deed must be followed. For example, if the deed contains a form that must be used, that form must be used. If the trustee must acknowledge the nomination, then we must have evidence that the trustee has issued an acknowledgement.

We are starting to see cases where the validity of binding nominations are being tested, and I see this continuing to be a battleground for estate litigators given the substantial wealth in superannuation. I have given a number of advices where superannuation trustees can ignore a document that was designed to be a binding nomination because it did not comply with the terms of the trust deed.

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2 see the Commissioner for Taxations comments in SMSF Determination 2008/3 and Ioppolo v Conti [2015] WASCA 45 and Munro v Munro [2015] QSC 61
3.6 In addition to the trust deed requirements, there are quite a number of technical requirements for a binding nomination to be effective for retail and industry superannuation funds set out in SIS Regulations 6.17A and 6.17B. In summary, these are:

(a) the trustee must give sufficient information to the member so the member understands the member’s rights to make a binding nomination;

(b) the nominees must be dependants of the member or the member’s legal personal representative;

(c) the proportion that is payable to each nominee is certain or readily ascertainable;

(d) the nomination is in writing, signed by the member in the presence of two witnesses who are over 18 and not mentioned in the nomination; and

(e) the trustee must advise the member each year that the member has made a binding nomination, who are the nominated beneficiaries and when it lapses.

The trustee also has an obligation to clarify a nomination if the nomination is not sufficiently clear to allow the trustee to pay a benefit.

3.7 Further, in a retail/industry superannuation fund the nomination is only binding for a maximum of three years (compare this to SMSFs), at which time the nomination lapses and is no longer binding on the trustee. If a beneficiary wishes to continue with the binding nomination, then they will have to make a new one.

3.8 A binding nomination can be changed at any time, so when you review a Will you should consider whether the client should have one or not, and whether you should change any existing one.

3.9 Even though retail and industry superannuation funds may provide the same opportunity to make binding nominations, practically the attitude of professional superannuation trustees in my experience limits the estate planning opportunities. For example, most retail and industry superannuation funds do not allow you to make cascading or conditional nominations. This effectively removes the majority of the tools out of any estate planner's toolkit.

**Binding nominations and SMSFs**

3.10 As the legislative provisions have no bearing on the binding nomination process in SMSFs, the provisions of the trust deed are paramount.

3.11 As discussed at paragraph 3.5, the process specified in the trust deed must be followed precisely. Where the process is not followed precisely, the nomination will not be binding on the trustee and it is highly likely, given the prevalence of estate litigation, to find this the subject of a challenge.

3.12 As binding nominations in SMSFs are purely a trust deed concept, they are not subject to the maximum three year validity that applies to binding nominations for retail and industry superannuation funds (see regulation 6.17A(7) of the SIS Regulations, SMSFD 2008/3, Ioppolo v Conti\(^4\) and Munro v Munro\(^5\)). Therefore, unless there is a restriction in the SMSF trust deed, it is possible to make a non-lapsing binding nomination in an SMSF.

3.13 Also, when preparing binding nominations for an SMSF it is possible to utilise your drafting skills so that the binding nomination can cover a multitude of situations. Unlike in the majority of retail and industry superannuation funds, the trustee will accept cascading or conditional nominations. Commonly, SMSF binding nominations even specify the form in which the death benefit is paid to the beneficiary.

\(^4\) [2015] WASCA 45
\(^5\) [2015] QSC 61
I have even seen situations where complex restrictions are placed on the payment of a death benefit pension to ensure that a ‘spendthrift’ surviving spouse does not have access to all the money.

**Binding nominations – When to consider?**

3.14 As mentioned above, the trustee’s discretion in relation to the payment of superannuation death benefits can be a very powerful tool as it is the only estate planning decision that can be made in hindsight. However, there are many cases where this lack of certainty and wide flexibility can be a serious problem.

3.15 This issue has been dealt with in detail in a great number of papers and is a subject entirely of its own. It is not the purpose of this paper to discuss this issue in detail, however a binding nomination will be particularly important where:

(a) it is not possible to adequately control the decision making process where a death benefit is payable (especially in a retail or industry superannuation fund);

(b) there is no appropriate person to make the death benefit decision;

(c) there is a risk of a dispute or a disagreement between the controllers of the superannuation fund following death;

(d) there are multiple families and you want your superannuation to be paid to a particular family member (rather than another – for example to children from any of your marriages instead of your current spouse);

(e) there is a high risk of your wishes not being implemented by the controller of the SMSF; and

(f) there is likely to be an argument between possible beneficiaries as to what will happen with your superannuation benefits.

This is a non-exhaustive list but provides examples of the more common situations where a binding nomination should be considered.

3.16 The disadvantage of a binding nomination is the loss of flexibility in being able to have the benefit paid to the appropriate person based on the situation at the time. This can be very important as your circumstances change - your binding nomination (unless it lapses) will not keep up with what is happening in your life.

3.17 This is why I do not recommend binding nominations as a matter of course – a binding nomination can be very useful in the right circumstances but the usefulness needs to be weighed against the loss of flexibility.

3.18 Given these issues, there is no universal answer for death benefit planning – for many people the flexibility inherent in superannuation is very important and useful, and for others the ability to lock in the payment is vital.

**Binding nominations – To the estate?**

3.19 If you do recommend a binding nomination be implemented, there is no such thing as a ‘default’ or ‘fall back’ beneficiary choice, this includes the estate.

3.20 The choice of beneficiary under a binding nomination must be the result of in-depth thought and analysis, even more so than any discussion around receipt of superannuation death benefits as the result of desired use of trustee discretion. This is because you are removing the trustee’s discretion and lose the ability to deal with the varying range of possibilities that might exist at the time of death.
It is the job of the advisor who recommends the binding nomination to carefully consider the probability of all situations and weigh up the pros and cons for making a binding nomination in a particular form.

3.21 It is almost negligent to recommend a binding nomination in favour of the estate where there is a risk of an estate challenge. It is an applicant’s solicitor’s dream for the size of the estate (except in NSW where the notional estate concept applies) to be increased by a significant superannuation death benefit payment.

3.22 Also, it is not desirable for superannuation to be paid to the estate where there is a concern or a likelihood of the estate being insolvent but for the superannuation death benefit.

3.23 Further, it is unlikely that the estate will be the default option where the superannuation death benefit is to be paid to a surviving spouse as it is generally desirable to maintain the death benefit in the superannuation system by paying the death benefit as a pension. However, this does not mean that a binding nomination to the surviving spouse is the default option where they are the intended recipient – this is generally for the same reasons as set out above. Despite this, I continue to see a number of advisors have every person who walks through the front door of their office sign up to a binding nomination to the surviving spouse without thinking through the consequences. The amount of times I have had to take urgent remedial action to revoke a binding nomination in favour of a spouse at high risk of litigation (professionals, directors, business owners, surgeons etc.) continues to astound me.

3.24 Despite this, there are situations where we ultimately want the superannuation to form part of the estate. I have discussed these situations in paragraph 5.

**Binding nominations – Make sure they have the intended outcome**

3.25 Once the decision is made to make a binding nomination, it is essential that careful consideration is given to the terms of the trust deed to ensure that the binding nomination has the intended outcome.

3.26 In paragraph 4, I outline the common issues I see that can affect the validity of a binding nomination and give rise to a challenge.

3.27 However, there are a few other common mistakes which do not result in the binding nomination being invalid, but merely impact on the effectiveness of the binding nomination.

*Entire member benefits*

There are a number of trust deeds where the operative provision only allows the binding nomination to deal with benefits in an ‘accumulation account’.

Therefore, any amount in a pension account will possibly not be subject to the binding nomination. However, this is not entirely clear and there is an argument that the amounts in pension accounts are commuted and form part of the accumulation account following the death of the member.

*Payment priority*

One of the more common debates in the superannuation industry at the moment is whether a binding nomination takes precedence over a reversionary pension. A reversionary pension is a pension that is being received by a member of a superannuation that expressly provides that the pension is to continue to another nominated person on the death of that member.

This issue is once again governed by the terms of the trust deed for the superannuation fund. Any good trust deed should clearly specify the order of priority if there is both a binding nomination and a reversionary pension.
Ordinarily superannuation trust deeds provide that a reversionary pension takes precedence over a binding nomination. The reasoning behind this is that, if the pension is taken to automatically continue under the reversionary pension rules, it never forms part of the death benefit to be dealt with by the binding nomination.

However, this is not always the case. There are many trust deeds that provide that a binding nomination overrides any reversionary pension or are silent on which takes priority. The latter situation is particularly problematic as without clear guidance in the trust deed there is the risk of having competing beneficiaries.

4. CHALLENGING THE VALIDITY OF BINDING DEATH BENEFIT NOMINATIONS

4.1 To be honest, I am surprised that we have not seen more cases where binding nominations have been the subject of the estate litigation, particularly given the number of times I have provided advice to SMSF trustees that a particular ‘binding’ nomination was not in fact ‘binding’ on the trustee.

However we have recently seen a few cases where the validity of a binding nomination was in question. Given that the large amount of money held in superannuation which can be effectively diverted from an estate challenge (except in New South Wales where the notional estate concept applies), I see this becoming a key battleground for estate litigators.

4.2 As highlighted throughout this paper, it is critical for a binding nomination to be made in accordance with the requirements in the trust deed. This is where the majority, if not all, of the challenges to a binding nomination are going to come from.

Common mistakes when implementing binding nominations

In my experience, practitioners generally make the same common mistakes when implementing a binding nomination. Although in-depth discussion of the issues is a topic in itself, the following are what I consider to be the common mistakes made by practitioners that could give rise to questions in relation to the validity of a binding nomination.

Approved form

There are a number of common trust deeds in circulation that require the binding nomination to be made in the ‘approved form’.

(a) Usually, this requires the member to use the specific form set out in the schedule to the particular trust deed. In the grand scheme of things, this is a fairly basic condition to satisfy, but it is surprising how many times it is not.

In most of these situations, I cannot be sure of the reasons why this requirement has been overlooked. However, the most compelling reason seems to be that the specified form did not have sufficient flexibility to cater for the practitioner’s drafting style (for example, it was not possible to make cascading nominations).

Unfortunately, where the ‘approved form’ is not used, it is irrelevant how well the alternative form is drafted, as it will not be binding on the trustee.

As mentioned many times in this paper, the provisions of the trust deed are of paramount importance. Where they are not complied with, there is no room for movement. Unlike in the world of drafting a Will, there is no such thing as substantial compliance or testamentary intention.

Therefore, if the trust deed requires a certain form to be used, that is the only form in which a binding nomination can be made and be binding on the trustee.

If you do not like it, amend the trust deed, not the form.
(b) In my opinion, an even bigger problem is caused by trust deeds that require the binding nomination to be made in the form ‘approved’ by the trustee.

These trust deeds do not usually include a default or pre-approved form and it is therefore up to the trustee to decide at the time what is the ‘approved form’. As a result, the trustee must have taken an active step to ‘approve’ a form before a nomination can be binding on the trustee.

Even where this step is taken by the trustee, such provisions are at high risk of a challenge. This is because if put to proof, the parties will need to produce evidence that the trustee ‘approved’ a form and that the form of the binding nomination used was in fact the ‘approved form’.

To date, not one client or advisor has been able to produce sufficient documentary evidence to show me that this requirement was satisfied where a client has made a binding nomination under a trust deed with such a provision.

As a result, I personally do not like to gamble on clients keeping adequate records to prove this issue if challenged. For this reason, I am inclined to vary trust deeds to remove this requirement when making a binding nomination even though it is technically possible to make a valid binding nomination under such provisions.

**Eligible beneficiaries**

Another common mistake is that the binding nomination nominates a beneficiary that is either:

(a) not an eligible recipient for the purposes of the *SIS Regulations*; or

(b) they are an eligible recipient for the purposes of the *SIS Regulations* but the trust deed provisions (in particular the definitions) are inexplicably narrow.

A common example that arises is where a person makes a binding nomination in favour of their de-facto spouse but the trust deed defines a ‘spouse’, for the purposes of the ‘dependant’ definition and the binding nomination clause, to only include a married spouse. In this case, the binding nomination to the de facto would not be valid as they are not a permitted beneficiary under the trust deed.

In one prominent superannuation trust deed, a binding nomination can only be made to a dependant and not to the estate.

Therefore, it is critical that the terms of the trust deed, including every relevant definition, are carefully considered when making a binding nomination to ensure that it is valid.

Also, it is critical that the binding nomination itself correctly refer to the intended beneficiary. As the power to make binding nominations for SMSFs is solely based on the provisions of the trust deed, the Courts have insisted on strict compliance with the requirements of the trust deed when determining the validity of binding nominations.

In the recent Queensland Supreme Court case of *Munro v Munro*[^6] the binding nomination was found to be invalid, allowing the trustees of the SMSF to distribute the deceased’s death benefit other than as set out in the nomination. The Court held the binding nomination was not valid as it did not comply with the requirements in the trust deed. The Court emphasised that the binding nomination would only be binding if it strictly complied with all the requirements of the trust deed. In this case, the nomination was to the ‘Trustee of Deceased Estate’ rather than the deceased’s ‘legal personal representative’ as required by the trust deed and the *SIS Act*. The Court determined that this was not a nomination of the deceased’s ‘legal personal representative’ (as required by the trust deed) as the roles were different.

[^6]: [2015] QSC 61,
Eligibility to make a binding nomination

This issue is a twist on the situation in the section above.

It is dangerous to assume that every member of a superannuation fund is able to make a binding nomination.

I have seen SMSF trust deeds which allow a ‘member’ to make a binding nomination, although, the definition of ‘member’ did not include a person whose only interest in the SMSF was their pension account. As a result of this drafting oversight, only a person with an accumulation balance in the superannuation fund could make a binding nomination.

Trustee acknowledgement

Another common binding nomination provision requires the trustee to ‘acknowledge’ the binding nomination for it to be valid and binding on the trustee.

Although this is not a difficult provision to comply with, I believe such provisions are high risk. If there is a dispute, the parties will need to produce evidence that the trustee ‘acknowledged’ the binding nomination. In my experience this step is not often completed satisfactorily, or where it has been attended to, the client does not keep adequate records to establish this at the time of payment of the death benefit.

Also, this clause presents a problem where the trustees/members have separated and one of the members wishes to make a new binding nomination. As the nomination has to be acknowledged by the trustee, you have to get the ex-spouse to consent to the new binding nomination for it to be valid. As you can imagine, this can be rather difficult.

Information to members

A similar issue arises where the trust deed requires the trustee to provide information to the member before they can make, or before the trustee can accept, a binding nomination. The following is an example of such a clause:

Information to Member: Before the Trustee accepts a Binding Death Nomination, the Trustee must give the Member a statement that...

Required compliance

Another critical mistake that I often find is that the binding nomination clause and the death benefit provisions in the trust deed do not work together.

Usually, the problem arises because the death benefit provisions do not ‘require’ the trustee to pay the death benefit in accordance with the binding nomination made by the member. The following is an example from a well-known trust deed:

Where this Deed provides for the payment of a Benefit on the death of a Member, the Trustee may pay or apply the Benefit to or for the benefit of the Nominated Dependants...

As you can see, this clause provides the trustee with a choice to follow the binding nomination or pay the death benefit in accordance with the trustee’s discretionary power. As a result, for the binding nomination to be ‘binding’ this clause needs to be amended.

Also, do not be surprised to see trust deeds where the death benefit provisions do not even refer to the binding nomination at all. In this case, depending on the exact wording of the binding nomination clause, it is likely that the binding nomination will not remove the trustee’s discretion in relation to the payment of the death benefit.
Compliance with the SIS Act & SIS Regulations

By far the most common issue that arises in SMSF trust deeds, including trust deeds from extremely reputable and experienced providers, is where the binding nomination provisions require the binding nomination to comply with the requirements of the SIS Act or SIS Regulations.

(a) In my experience, these provisions usually present in one of two forms:

(i) The definition of binding nomination in the trust deed refers to a binding nomination ‘made in accordance with section 59(1A) of the SIS Act’.

(ii) The operative clause in the trust deed requires the binding nomination to comply with section 59(1A) or regulation 6.17A (or both) for the trustee to be bound.

As mentioned earlier, neither the SIS Act nor the SIS Regulations provisions relating to binding nominations apply to SMSFs. Therefore, in my view, the trustee of the SMSF will not be bound by the binding nomination where the trust deed requires the binding nomination to comply with or be binding under the SIS Act or SIS Regulations.

This is contrasted to a provision that does not require compliance with section 59(1A) or regulation 6.17A but merely imports the technical requirements set out in those provisions into the trust deed.

(b) This issue was the subject of the dispute in the case of Donovan v Donovan. In this case, the deceased (Mr Donovan) was a member of the SMSF and a director of the trustee company. The operative provision that allowed the member to make a binding nomination was clause 11.4(b) of the trust deed, which provided as follows:

A member may make a binding death benefit nomination in the form required to satisfy the Statutory Requirements;

The trust deed provided as follows:

(i) ‘Statutory Requirements’ was defined widely to include ‘any law…which must be satisfied by a superannuation fund in order to qualify for income tax concessions…’.

(ii) Where a member had made a valid binding nomination, the trustee must pay the death benefit to the nominated legal personal representative or dependant of the member.

The deceased purported to make a nomination by letter to the trustee which specified that he wanted his benefits paid to his legal personal representative for inclusion in his estate assets.

The deceased’s second wife and a child of the deceased’s first marriage, who were the deceased executors, were disputing whether this was a valid binding nomination that had to be followed by the trustee. The second wife argued that the nomination was binding on the trustee.

However, the deceased’s children argued that the nomination was not binding for two reasons:

(i) Firstly, the language used was not sufficient to convey a binding intention. The nomination merely indicated that the deceased ‘wished’ for his death benefit to be paid in a particular way, not required or directed.

(ii) Secondly, the nomination was not sufficient to comply with the requirements of the ‘Statutory Requirements’.

In addition to these issues, Fryberg J raised the issue of the ‘approved form’, but neither party pursued this issue and, in any event, it was irrelevant to the end result.

Fryberg J dealt with the second issue first and held that the reference to ‘Statutory Requirements’ for the purposes of the binding nomination provision was a reference to the formalities in regulation 6.17A(6) of the SIS Regulations as to read the clause in the trust deed in any other way would render the provision meaningless.

The formalities in the SIS Regulations required the nomination to be in writing, witnessed by two persons and contain a signing declaration from the witnesses in relation to the signing of the nomination.

The letter written by the deceased to the Trustee clearly did not comply with the requirement of regulation 6.17A. As a result, the nomination was not binding on the trustee.

Further, the judge ordered that the costs of the dispute be paid from the estate on an indemnity basis.

4.3 This position was affirmed by the Queensland Supreme Court in Munro v Munro\(^8\) were they held that a binding nomination in relation to benefits in a SMSF does not have to comply with the requirements in the SIS Act and SIS Regulations (unless the trust deed requires that).

4.4 As you can see, the majority of these issues result from the wording of the trust deed and can be overcome by replacing the binding nomination provisions with a provision with more user-friendly drafting. When I am preparing a binding nomination, more often than not I replace the binding nomination provisions to remove the possibility of having a dispute in relation to the above issues.

4.5 However, the recent case of Wooster v Morris\(^9\) demonstrates that practitioners must think beyond the binding nomination when advising on superannuation death benefits.

This case involved a challenge to the validity of the binding nomination. The judgment does not examine this issue as the binding nomination was found to be valid by a special referee before the hearing. However, the case demonstrates that even where there is a binding nomination, it is critical to ensure that the correct person will be running the superannuation fund in the event of the death of a member. I have discussed this issue in detail in paragraph 7 below.

4.6 Another concerning issue is the manner in which practitioners initially respond to a dispute where there is challenge to the superannuation death benefit. Quite often, where there is a binding nomination in existence, the practitioners are very quick to write a response to the claimant notifying the claimant of the binding nomination and the fact that the death benefit has been paid in accordance with that nomination.

I understand the reasons for this, as it is usually a very quick way to dismiss the dispute.

However, such a statement must not be made lightly and should only be made after a thorough review of the binding nomination and the trust deed.

If such a statement is made and the binding nomination is not in fact ‘binding’, the actions of the trustee in paying the death benefit could be subject to the challenge.

\(^8\) [2015] QSC 61,
\(^9\) [2013] VCS 594.
Challenging the trustee’s actions/discretion

4.7 It is the general trust law position that the discretionary powers of a trustee are not generally subject to review and therefore, there is very limited scope to challenge the exercise of a discretion.

This issue is extremely complex and is not the subject of this paper. However, when such a discretionary power is exercised, the trustee must inform themselves of all the relevant matters regarding the exercise of a decision.

Where it can be established that the trustee has not considered all relevant issues, it is possible for the original decision to be set aside. It is for this reason that the preferred position is not to provide reasons for the exercise of a discretion.

In the situation discussed in paragraph 4.6, if the binding nomination is not valid, the reasoning supporting the payment of the death benefit to the claimant is flawed and can be the subject of a challenge. That being said, it is often not worth challenging these issues as the Court usually refers the decision back to the trustee to be re-determined.

This issue should also be considered when a claimant asks whether they were a considered beneficiary for the purposes of the death benefit payment. Great care needs to be made when responding to such claims to avoid adding fuel to the fire.

4.8 For retail and industry superannuation funds, the common law position has been modified by the Superannuation (Resolution of Complaints) Act 1993 which allows a person to complain to the Superannuation Complaints Tribunal for a review of the exercise of a trustee’s discretion.

5. DEATH BENEFITS PAID TO THE ESTATE – WHEN IS IT APPROPRIATE?

Determining the most appropriate beneficiary

5.1 Determining the most appropriate beneficiary of the death benefit, whether it be the estate or some other dependant, is always a difficult matter and involves the weighing up of a number of pros and cons.

Where this decision can be made by the (appropriate) trustee after the death of the member, it is substantially easier. However, as discussed in paragraphs 3.19 to 3.24, where a binding nomination is being prepared in anticipation of a member’s death, the task is so much harder as the probability of certain events (for example, an estate challenge) has to be considered and factored into the decision making process.

5.2 The main situations where we want the superannuation death benefit to be paid to the estate include where:

(a) the person we want to receive the superannuation death benefit is not an eligible beneficiary for the purposes of the SIS Regulations (for example, a sibling or friend);

(b) it is desirous for the superannuation death benefit to form part of a testamentary trust for a dependant or non-dependant for any of the usual reasons – for example, asset protection, tax planning or other control purposes; or

(c) the person we want to receive the superannuation death benefit is not a ‘death benefits dependant’ for the purposes of the Income Tax Assessment Act 1997 as it is possible for there to be a substantial tax saving (see the table below) where the superannuation death benefit is paid to beneficiary through the estate rather than directly.
### Superannuation & Wills – May 2015

#### 5.3 However, even where these are desired outcomes, it is not appropriate to pay the superannuation death benefit to the estate in the following situations:

(a) There is the possibility of estate challenge. It is possible for the trustees, where there is no binding nomination or other restricted death benefit provision, to use their discretion to wait until the time limits for making an estate challenge have passed and pay the superannuation to the estate after that risk is eliminated.

We have been involved in a number of situations where we have advised the trustees to wait until both the 6 and 9 month time periods have passed before exercising their discretion to pay the death benefit to the estate.

This does not apply in New South Wales where the ‘notional estate’ concept applies when challenging an estate.

(b) The Will does not including appropriate clauses to manage the potential tax liabilities effectively – see the discussion in paragraph 6.

(c) Where there is a risk that the estate will not be solvent.

(d) You can pay the death benefit as a pension to the desired beneficiary. The SIS Regulations permit the death benefit to be paid as a pension to the surviving spouse and in certain situations to the children of the deceased.

Where this is possible, it is generally desirable to pay a pension to the eligible recipient as the superannuation death benefit remains in the superannuation system and therefore continues to be concessionaly taxed.

Where a child is the desired recipient, this tax benefit needs to be weighed against the fact that the superannuation death benefit pension must be paid out of the superannuation system when the child turns 25, unless they are disabled.

#### Superannuation death benefit testamentary trusts

5.4 There are many situations where it is desirable for estate assets and superannuation death benefits to form part of a testamentary trust. It is not the job of this paper to talk about when it is appropriate to use a testamentary trust or the ins and outs of testamentary trusts generally.

5.5 Quite often as indicated above, where superannuation is to form part of the estate, the primary reason is so that it forms part of a testamentary trust.
5.6 Where this is the case, it is important that the terms of the testamentary trust properly deal with the implications of receiving superannuation death benefits.

5.7 Even though it is possible to have a testamentary trust with a very limited range of beneficiaries, most testamentary trusts these days have a wide range of beneficiaries so that the trust is more tax effective.

However, testamentary trusts with wide clauses of beneficiaries can inadvertently result in tax being payable where the assets of the testamentary trust include a superannuation death benefit. This is because the tax treatment of the superannuation death benefit depends on the extent that tax law dependants are likely to benefit from the superannuation death benefit.

Where there is a mix of tax law dependant and non-dependant beneficiaries and the trustee has a wide discretion, it is unlikely that the tax benefit in section 302-10 of the *Income Tax Assessment Act 1997* will apply and the estate will be taxed as if the death benefit is paid to a non-dependant.

It is possible to draft the testamentary trust deed so that the concessional tax treatment is maintained where the testamentary trusts includes dependant beneficiaries – see paragraph 0.

Where you have a mix of dependant and non-dependant beneficiaries, this is an important consideration as the tax treatment is substantially different:

<table>
<thead>
<tr>
<th></th>
<th>Payment to estate and then to a death benefits dependant</th>
<th>Payment to estate and then to a non-dependant</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Tax on tax free component</strong></td>
<td>Tax free</td>
<td>Tax free</td>
</tr>
<tr>
<td><strong>Tax on taxable component (taxed element)</strong></td>
<td>Tax free</td>
<td>Taxed at flat rate of 15%</td>
</tr>
<tr>
<td><strong>Tax on untaxed element</strong></td>
<td>Tax free</td>
<td>Taxed at flat rate of 30%</td>
</tr>
<tr>
<td><strong>Tax liability</strong></td>
<td>Nil</td>
<td>Legal personal representative (from estate)</td>
</tr>
</tbody>
</table>

6. **WILL CLAUSES AND SUPERANNUATION DEATH BENEFITS**

6.1 Any well drafted Will should deal with the possibility of a superannuation death benefit being received even where active steps have been taken as part of the planning process to divert the superannuation away from the estate. This means that appropriate clauses need to be inserted to deal with the possibility and the vast range of potential consequences that could apply should a superannuation death benefit form part of an estate.

In the absence of such clauses, opportunities to maximise the estate assets will be lost which could potentially result in disgruntled beneficiaries and possibilities of allegations of negligence against the practitioner who assisted with the estate planning.

6.2 In my opinion, you should consider the inclusion of the following clauses in any Will you prepare.
Equalisation clause

Where the superannuation death benefit is intended to be split between multiple beneficiaries either directly or through the estate – for example, to the surviving children – it is essential that the Will include an ‘equalisation clause’.

An ‘equalisation clause’ is designed to increase the portion of the estate assets left to the beneficiary who does not receive the superannuation death benefit and decrease the portion of the estate received by the beneficiary who does. This ensures that the total share of the deceased’s assets (including the estate assets and the superannuation death benefit) left to each beneficiary is equal. The clause is designed to prevent one beneficiary receiving a windfall by taking the superannuation death benefit directly from the fund and then still sharing equally in the estate assets under the Will.

It is critical that this clause be included where the superannuation trustee will have a discretion as to what is to happen to the superannuation death benefit, however, it should also be included where there is a binding nomination, reversionary pension or specifically drafted death benefit clause in the trust deed. This is because, like all well-made plans, something may change.

A perfect example of where this clause may have been useful was in the case of *Katz v Grossman.* In that case, the daughter of the deceased was the co-trustee of the SMSF and decided to pay the superannuation death benefit to herself rather than equally between her and her brother or to the estate. As a result, the daughter received a significantly larger share of the assets than her brother.

However, it is important to note that ‘equalisation clauses’ have some limitations. In particular, for the equalisation clause to work perfectly and equalise the total benefits left to each beneficiary, there have to be sufficient assets in the estate. For example, where there are two beneficiaries to benefit equally, the estate assets have to be worth at least the same amount as the superannuation death benefit. Where there are three beneficiaries, the estate assets have to be worth at least twice as much as the superannuation death benefit.

Dependants’ clause

It is my view that a Will should be drafted to minimise the tax payable on the superannuation death benefit if it is an estate asset.

To achieve this, the Will should include a ‘dependants clause’ which allows the executors to allocate specific assets to specific beneficiaries (or their testamentary trusts). The clause should be worded widely enough to allow the executors to allocate the superannuation death benefit, to the extent possible, to the dependant (for tax law purposes) beneficiaries to minimise any tax payable, with other estate assets going to the non-dependant beneficiaries.

This clause can result in substantial tax savings and therefore an increase in the total estate assets for the beneficiaries. I have seen this clause work extremely well where the estate is left to the deceased’s children but only one of them is a ‘dependant’ for tax law purposes.

In the absence of a specific clause empowering the executors to do this, the estate assets will be proportionately split between the beneficiaries and this could result in a beneficiary having to pay tax on the portion of the superannuation death benefit they receive where they are a non-dependant.

Streaming clause

A further extension of the ‘dependant’s clause’ is a clause that allows the different components of a superannuation death benefit to be streamed to different beneficiaries. By different components, I mean the taxable, tax-free and untaxed components that usually make up a superannuation death benefit payment.

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10 [2005] NSWSC 934
It is well known that where a superannuation death benefit is paid by a superannuation fund, each payment includes a proportionate amount of each component and it is not possible to pay different components separately to different beneficiaries. This is desirable where there are both dependant and non-dependant beneficiaries as different tax consequences apply to each of the components.

However, where the superannuation death benefit is paid to the estate, it is arguable that the different components can be streamed to different beneficiaries. Under general trust law, it is possible for different income and capital amounts to be streamed where the trust deed provides that the different amounts retain their character and there is a clause which permits the different amounts to be streamed.

For this reason, I include a clause that allows the different components of the superannuation death benefit to be streamed to different beneficiaries. This allows the executors to allocate the tax-free component to the non-dependant beneficiaries so that no additional tax is payable and the taxable component to the dependant beneficiaries so that no tax is payable on that amount.

**Sub-trust clause**

As discussed in paragraph 5.7, it is common for superannuation death benefits to form part of a testamentary trust with a wide class of beneficiaries that includes dependants and non-dependants (for tax law purposes).

Without the inclusion of a specific clause in the terms of such a testamentary trust, tax will be payable on the superannuation death benefit by the estate as if it was paid to a non-dependant beneficiary – this is the case even if practically the trustee of the testamentary trust will only distribute to the dependant beneficiary. This is because the superannuation death benefit is only concessional taxed to the extent the dependant beneficiary is likely to benefit (section 302-10 of the *Income Tax Assessment Act 1997*).

Therefore, the terms of the testamentary trust should include a ‘sub-trust clause’ which holds the superannuation death benefit on trust solely for the benefit of the dependant beneficiaries and only where there are no dependant beneficiaries, can the superannuation death benefit be paid to the non-dependant beneficiaries.

If one of the beneficiaries of the testamentary trust is a ‘dependant’ for tax law purposes at the time the estate is distributed, then it is my opinion that the superannuation death benefit will be taxed as if it were paid to a dependant under section 302-10 *Income Tax Assessment Act 1997* where such a clause is included.

**Conflict Clause**

In light of the recent decision in the Queensland case of *McIntosh v McIntosh*, I believe additional caution needs to be taken where the desired recipient of the superannuation death benefit is also the executor (or potentially the administrator) of the estate.

One possible step that can be taken to address the issue in *McIntosh* is to include a conflict clause in the Will that expressly authorises the executor to also pay, or apply to receive, the superannuation benefits personally.

I have addressed the *McIntosh* case and its importance to the way we approach estate planning in detail in paragraph 8.

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11 [2014] QSC 99
7. CONTROL OF THE FUND AFTER DEATH

Importance of who controls the fund

7.1 The issue of the ‘control’ of the superannuation death benefit decision is deeply embedded in the minds of most estate practitioners.

7.2 The importance of who controls the superannuation fund and has the discretion as to how the superannuation death benefit is paid was highlighted by the case of Katz v Grossman. In this case, Daniel Katz brought an action against his sister Linda Grossman and her husband Peter Grossman claiming an interest in their father’s SMSF. The key facts of this case were as follows:

(a) The deceased and his late wife were individual trustees of their SMSF.
(b) The deceased’s wife died in 1998 and the deceased appointed his daughter Linda as an additional trustee of the fund.
(c) When the deceased died in 2003, Linda appointed her husband Peter as a co-trustee.
(d) The deceased had made a non-binding nomination of beneficiary in which he indicated that he wanted his superannuation benefit to be divided equally between Daniel and Linda.
(e) Linda and Peter refused to follow the deceased’s non-binding nomination and decided to pay the entire benefit of approximately $1,000,000 to Linda.
(f) Daniel challenged the appointment of Linda and Peter as trustees of the fund.

The Court held that both Linda and Peter were validly appointed as trustees and as a result they were entitled to exercise the powers of the trustee. This included the discretionary power to pay the death benefit in accordance with the trust deed and the SIS Regulations.

7.3 Following this case, practitioners generally paid a lot more attention to binding nominations and who had the power to control the superannuation fund where there was no binding nomination to prevent such abuses from occurring.

7.4 Despite this, I do not think as much focus has been given to who controls the superannuation where the superannuation death benefit decision is locked in either by way of binding nomination, reversionary pension or specific trust deed provision. This is most likely due to the complacency resulting from the knowledge that the trustee has to comply with a pre-made decision.

Although the thought process behind this is logical, it does not necessarily prevent a dispute. The recent Victorian Supreme Court case of Wooster v Morris is a prime example of the potential issues that can arise where the trustee chooses not to comply with the trust deed.

In this case the deceased had made a binding nomination for the benefits in his SMSF in favour of his two daughters from his first marriage, who were also the executors of his estate. At the time of his death, the deceased’s second wife was the surviving member and trustee of the SMSF.

The second wife disputed the validity of the binding nomination and had obtained legal advice that the nomination was not binding as it was not delivered to her in her capacity as a co-trustee as required by the trust deed. The second wife, as the surviving trustee and the controller of the SMSF, therefore decided to pay the superannuation death benefit to herself.

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12 [2005] NSWSC 934
13 [2013] VSC 594
As a result, the daughters had to commence proceedings to obtain an order that the nomination was valid and binding on the trustee and to direct the second wife to account for the superannuation death benefit to them.

The judgment does not contain a detailed consideration of the reasoning why the binding nomination was valid, however, the daughters were successful. The Court also ordered that the daughters’ costs by paid by the second wife and the new corporate trustee of the SMSF and that the deceased’s superannuation death benefit was not to be diminished by the costs order.

7.5 In my opinion, this case demonstrates how critical it is to deal with the control of the SMSF in all situations, including where the trustee’s discretion is removed. Our clients will not thank us for the work we do if they have to go to Court to enforce their right to receive the superannuation death benefit under a binding nomination, reversionary pension or a specific trust deed provision.

7.6 Broadly speaking, the issue with control of SMSF can be broken down into two categories:

(a) SMSFs with individual trustees; and

(b) SMSFs with corporate trustees.

**Individual trustees**

7.7 Where there are individual trustees it is critical that you review the terms of the trust deed to determine how a replacement trustee is appointed in the event of the death of a trustee and member. This is because:

(a) the deceased will cease automatically to be a trustee on their death; and

(b) control of the SMSF will then rest with the remaining individual trustees and the person who has the power to appoint new trustees.

7.8 Where a member dies, section 17A(3)(a) of the SIS Act provides that the deceased’s legal personal representative (LPR) must be appointed as a trustee of the fund (or a director of a corporate trustee) within six months of the member’s death in order to satisfy the basic conditions to remain an SMSF whilst the deceased still has member benefits in the SMSF. If this is not done, the SMSF ceases to be a complying SMSF and can be made non-compliant by the ATO.

However, section 17A of the SIS Act does not automatically appoint the LPR as a trustee (or a director of a corporate trustee) of the SMSF. This is a common misconception.

7.9 The importance of reviewing the SMSF trust deed to determine who has the power to appoint trustees was addressed in the case of *Ioppolo & Hesford v Conti*.14

In this case, the deceased and her husband (possibly a second husband) were both the trustees and members of an SMSF. Prior to her death, the deceased had signed several non-binding and binding nominations directing that her superannuation death benefit be paid to her husband but these had lapsed.

Also, in her Will, the deceased directed that her superannuation be paid to her children and she expressed her wish that none of her benefit should be paid to her husband.

At the time of her death, the SMSF’s trust deed provided that unless there was a binding death benefit nomination, the trustee had absolute discretion as to how a death benefit was to be paid.

Upon death, her husband was left as the sole trustee of the SMSF. The husband subsequently changed the trustee of the SMSF to a company of which he was the sole director and

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14 [2013] WASC 389
shareholder. Presumably, this was to ensure that the requirements of section 17A of the *SIS Act* would continue to be complied with once the deceased’s death benefit was paid.

Following the change of trustee, the deceased’s husband exercised his power as the sole director of the corporate trustee to pay the deceased’s superannuation death benefit to himself, not to the deceased’s children.

The deceased’s children challenged this decision on the following grounds:

(a) they argued that the deed required the deceased’s LPR to be appointed as trustee of the SMSF because the deed required the fund to remain an SMSF; and

(b) the trustee did not exercise their discretion in good faith.

The second argument failed as the deceased’s husband had act prudently, including taking advice on his obligations in relation to paying the death benefit.

In relation to the first argument, Master Sanderson J reviewed the requirements of section 17A of the *SIS Act* and held that:

Section 17A(3) allows for the appointment of an executor as a trustee of the fund but does not in its terms require such an appointment.

Therefore, in the absence of any express clause in the trust deed, the Court found that the deceased’s husband was not required to appoint her LPR as a trustee, and therefore, the husband’s exercise of powers was valid.

7.10 Therefore, in order to pass control of the SMSF on the death of the member, the following issues need to be carefully considered:

(a) the choice of legal personal representative as the intention will be for this person to become a co-trustee and assist in the death benefit decision; and

(b) the provisions in the trust deed for appointing trustees.

7.11 The provisions in SMSF trust deeds for appointing trustees are many and varied. The most common trust deed provision for appointing trustees is a clause that requires the determination of a majority of members.

Although this provision may be sufficient for everyday operation, it can be the source of problems when it comes time to appoint the LPR as a trustee.

In your typical two member SMSF, this would require the consent of the surviving member (generally the surviving spouse), to have the LPR appointed as a trustee. This may be a problem where the interests of the continuing trustee/member and the LPR are not aligned (as in *Ioppolo v Conti*).

7.12 As a result, it may be necessary to think about alternative clauses for appointing trustees. For example:

(a) each member has the right to appoint a trustee; and

(b) following the death of a member the LPR of that member has the right to appoint themselves as a trustee.

7.13 Also, when reviewing or drafting trustee appointment clauses it is important that you are aware of the common drafting mistakes I see in SMSF trust deeds. These include the following:

(a) The deceased person ceases to be a member immediately on death even though their member benefits have not yet been paid. Sometimes this is clearly set out in the membership clauses, other times it occurs inadvertently as the member ceases being a
trustee and the trust deed provides that where a person ceases being a trustee they also cease being a member.

(b) The trust deed does not give the LPR the power to exercise the member’s rights. This can be a particular problem where you have a two member SMSF and the appointment clause requires a majority of members to approve the appointment. As no one is entitled to vote on the deceased member’s behalf, it is not possible to appoint a new trustee.

This can also be a problem in single member SMSFs as well. Although, the Trusts Acts in the various states are usually of assistance where this issue arises.

(c) The trust deed contains a restrictive definition of legal personal representative.

7.14 Even where these issues have been addressed, one issue is often overlooked. That is the ‘timing gap’ between the date of a member’s death and when the substitute trustee is appointed.

Unless this issue is properly addressed, in my opinion, there is no point drafting a trustee appointment clause that is going to work for your client’s circumstances. This is because the surviving trustee can make the decision on where to pay the superannuation death benefit before the substitute trustee is appointed in place of the deceased member.

7.15 To address this issue, some prominent SMSF trust deed providers include a clause that automatically appoints the LPR of the member as a trustee of the SMSF on the member’s death.

Although the logic behind this clause is obvious, I am concerned that in the majority of cases it will not operate as intended. This is because section 118 of the SIS Act provides as follows:

A person is not eligible for appointment as a trustee of superannuation entity, or as a director of a corporate trustee of a superannuation entity, unless that person has consented in writing to the appointment.

As a result, the automatic appointment clause will only apply to appoint the LPR as a trustee of a SMSF where they have consented prior to the death of the member. To date, I have never had a client who has been able to produce paperwork to prove this step has occurred. In the absence of this paperwork, the appointment of the LPR as a trustee will be invalid.

7.16 Other alternatives that you may wish to consider include the following:

(a) You could include a restriction on when the trustee of the SMSF is permitted to make the death benefit decision. For example, a clause could be included to prevent a death benefit payment decision being made within 30 days of the date of the member’s death. By including this restriction, you provide the LPR with sufficient time to be appointed as a trustee.

(b) The person who you want to ultimately control (or co-control) the SMSF could be added as a member and therefore a trustee of the SMSF at the time you are undertaking the estate planning. This will mean that there is no timing gap.

(c) The husband and wife each have their own SMSF with a corporate trustee. I have recommended this option on a number of occasions where there has been a blended family and control has been a real concern as they want the superannuation death benefit to go to their children rather than the surviving spouse.

Corporate trustees

7.17 Generally, the same issues arise where the SMSF has a corporate trustee, except that the:

(a) control of the deceased member’s shares (if they had any) in the corporate trustee needs to be addressed; and
power of appointing directors under the company constitution needs to be considered in addition to the trust deed provisions.

7.18 Passing control of the shares in the corporate trustee seems easy; however, it can often be more difficult than first thought. For example, leaving the shares to the intended recipient under the Will is effective except if the Will is the subject of an estate challenge.

Where passing control of the shares under a Will is likely to be problematic, you need to consider the other options available to ensure the correct people end up with the control. Some alternatives I have used in the past include the following:

(a) Transfer the shares in the corporate trustee so that the SMSF member and the intended controller after the member’s death jointly own the shares in the corporate trustee. Under the rules of survivorship, the member’s interest in the shares will automatically pass to the other joint owner on the member’s death.

(b) Issue a different class of shares (for example an A class share) to the intended controller of the corporate trustee after death. These ‘A Class’ shares are set up to have no voting rights whilst the SMSF member is alive, however, the constitution provides that on the death of the member, the voting rights on the ordinary shares cease and the ‘A class’ shares automatically become voting shares.

7.19 However, even if the control of the deceased’s shares in the corporate trustee is adequately dealt with under the Will, it is also necessary to consider the provisions in the constitution for appointing directors. The majority of constitutions follow the Corporations Act replaceable rule\(^\text{15}\) that a majority of member eligible to vote at a general meeting is required to appoint a director.

This position gives rise to the same issues outlined in paragraphs 7.11 and 7.14.

Generally the options discussed in paragraphs 7.12 and 7.15 can be used to overcome this problem if appropriately worded clauses are included in the company constitution.

7.20 In addition to these solutions, you may want to include a restriction on the directors of the corporate trustee making a death benefit decision, similar to that discussed in paragraph 7.16(a). A common provision that I have used in SMSF corporate trustee constitutions is one that requires:

(a) a majority or unanimous resolution of shareholders to approve a death benefit payment; or alternatively

(b) a particular class of shareholder (this works well when different classes of shares have been issued to each member) to approve the death benefit decision.

It is my preference to draft these clauses to give the shareholders the overriding power rather than the directors, as it is easier to pass control of the shares automatically on death than automatically appointing a trustee or a director or including some other restriction on when a trustee or a director can make a death benefit payment decision.

\(^{15}\) see section 201G of the Corporations Act 2001
7.21 Where the SMSF member does not hold shares in the corporate trustee, there are generally two options:

(a) include a specific clause in the company constitution that allows the LPR of the member to appoint themselves as a director; or

(b) give the LPR the ability to appoint themselves as a co-trustee with the company under the trust deed.

Other control issues

7.22 There are some additional control issues that I believe should be considered when advising clients on control of their SMSF as part of their estate planning.

Weighted voting

7.23 There are a significant number of specialist SMSF trust deed providers that now include clauses in the trust deed and corporate trustee constitution that weight trustee (except where trustees are required to act jointly), member and director voting powers in accordance with their member balance in the SMSF. The effect of such clauses is to provide the person with the highest member balance with control over the various decision making processes (assuming a two member SMSF).

Although such clauses may have some operational benefits, there are inherent risks that we as estate planning practitioners must warn our clients of.

My main concern is that clients are not warned of the consequences where they no longer have the largest member balance in the SMSF. This can be particularly problematic where the member dies as they may:

(a) no longer have the necessary voting power for their LPR to appoint themselves as a trustee or a director of the corporate trustee; or

(b) be able to appoint themselves as a trustee or a director, but the other trustee or director has sufficient voting power to make the death benefit payment decision by themselves without the LPR’s input.

LPR override

7.24 Recently, I have seen a worrying trend to include a clause in the SMSF trust deed to provide a member’s LPR (which includes their attorneys) with the power to amend, alter or otherwise change the member’s binding nomination whilst they are alive or at any time before the death benefit is paid.

In my opinion, these clauses are one step too far. Although the person appointed as the member’s LPR may be chosen after careful consideration, this gives the LPR the power to exercise a wide ranging power which could be used to their benefit. For example, there is nothing in these clauses that prevent the LPR from revoking a binding nomination in favour of another dependant and then using their trustee discretion (assuming they can validly appoint themselves) to make a death benefit payment that benefits them where they are a dependant.

Given the potential downside, it is essential that you warn clients of the risks with these clauses where they are included in the SMSF trust deed or corporate trustee constitution.

Capacity

7.25 Although a loss of capacity is not an issue that arises because of death, if a member of an SMSF losses capacity, this can be fatal to the operation of the SMSF.

Where a member losses capacity, they are no longer capable of acting as a trustee or a director of a corporate trustee. There are two potential problems that result:
(a) If the person is not automatically removed as a trustee or a director of the corporate trustee, it may not be possible for decisions to be made. This is particular a problem for two member funds as decisions either require unanimous or majority decisions – in a two member fund this will require both to consent to decisions.

(b) Where the trust deed or constitution provides that the person is automatically removed from their position in the event of incapacity, the SMSF may no longer continue to satisfy the basic requirements to be a complying superannuation fund. This is because section 17A of the SIS Act requires every member to be either a trustee of the fund or a director of a corporate trustee.

However, there is an exception to this rule which allows the member’s LPR to be appointed a trustee or a director in place of the member. This has to be done within 6 months of the member ceasing to be a trustee or a director. Although, you need to check the terms of the trust deed carefully as it may not permit the LPR to be appointed as a trustee or a director or a person to remain a member where they are not personally a trustee or director.

A person will be a LPR if they are the trustee of the member’s estate where they are under a legal disability or they are the member’s attorney appointed under an enduring power of attorney.

It is a common misconception that the enduring power of attorney document needs to authorise the attorney to act as trustee of the SMSF or give the attorney power of the member’s financial affairs. However, this is not correct. Section 17A(3) of the SIS Act merely provides that the SMSF will remain complying where a person who is appointed as a member’s attorney acts as trustee or director in the place of the member. Therefore, this section will be satisfied where a person who is only appointed in relation to personal and health matters acts as a trustee or director in place of a member.

If the member does not have a LPR who can be appointed as a trustee or a director of the corporate trustee, the SMSF is at risk of being made non-complying unless:

(i) the member’s benefits are rolled out (which will usually require assets to be sold) to a retail or industry superannuation fund; or

(ii) a APRA approved trustee is appointed.

Generally both these options are not desirable.

It is my view that it is critical (non-negotiable) that each person who is a member of a SMSF has an enduring power of attorney in place to avoid these issues.

8. **MCINTOSH v MCINTOSH – THE BIGGEST CHANGE IN ESTATE PLANNING SINCE…**

8.1 As I have discussed above, the discretion of the trustee of a superannuation fund to choose the recipient of a superannuation death benefit is a core principal central to estate planning, particularly where the benefits are in an SMSF.

8.2 But the Queensland case of *McIntosh v McIntosh* has called this into question.

8.3 In *McIntosh v McIntosh* the deceased died with no will, spouse, children or other dependants. His assets at the time of death were worth approximately $80,000 plus $450,000 of benefits in retail superannuation funds.

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16 Section 17A(3)(b) of the SIS Act
17 Section 17A(4) of the SIS Act
18 [2014] QSC 99
The deceased was survived by both his parents, who under the rules of intestacy in Queensland were the beneficiaries of his estate in equal shares. The parents had an acrimonious relationship even though they had been divorced for over 30 years.

The deceased’s mother applied for and was appointed administrator of his estate.

Following her appointment as administrator, the deceased’s mother applied to the retail superannuation funds for the deceased’s superannuation death benefit to be paid directly to her on the basis that she was in an interdependency relationship with the deceased. The trustees of the three retail superannuation funds accepted her claim and paid all of the deceased’s superannuation death benefit ($450,000) to her.

This substantially impacted on the benefit that was to be received by the deceased’s father who would only get approximately $40,000 from the estate, compared to $266,000 if the superannuation death benefit was paid to the estate. Consequently, the deceased’s father disputed the mother’s right to receive the payment of the superannuation death benefit directly.

To resolve the issue, the deceased’s mother applied to the Supreme Court for a direction that she did not have to account to the estate for the superannuation death benefit.

The deceased’s further argued that the deceased’s mother should have to account for the superannuation death benefit to the estate for the following reasons:

(a) The deceased’s mother appointed as the administrator of the estate by the Court and therefore had an obligation to gather in the assets of the estate.

(b) She also had a fiduciary obligation which required her to act honestly and in good faith for the benefit of the beneficiaries of the estate and not to allow a conflict of personal interest and duty to occur

(c) By applying for the superannuation death benefit personally, the deceased’s mother breached both the above duties.

8.4 Atkinson J agreed with the deceased’s father and ordered that the deceased’s mother account to the estate for the superannuation death benefits, as the ‘failure of the applicant to apply for payment to herself as legal personal representative was in breach of her fiduciary duty to act in the best interests of the estate, for which she may be held liable to the court.’

In arriving at this conclusion, Atkinson J relied on the following:

(a) The method of the appointment is an important distinction. An administrator is appointed by the Court whereas the ‘appointment of an executor is the act of the testator exercising testamentary choice.’

(b) There ‘is an exception to the general rule that no one who has fiduciary duties is allowed to enter into engagements in which the fiduciary has or may have a personal interest conflicting with the interests of those whom the fiduciary is bound to protect. The exception is described more precisely by Hope JA in Mordecai v Mordecai:

"That exception is where a testator or settlor, with knowledge of the facts, imposes on a trustee a duty which is inconsistent with a pre-existing interest or duty which he has in another capacity. In that situation the trustee is not thereby debarred from accepting the trust or from performing the duties which are imposed under it."

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19 [2014] QSC 99 at [78]
20 [2014] QSC 99 at [62]
The exception does not however extend to allowing a trustee, by the trustee’s own act, voluntarily to put himself or herself into a new position of conflict. 22

(c) Although there is an exception to the fiduciary’s obligation to avoid conflicts, Atkinson J held that it does not apply where the person administering the estate is appointed by the Court. This is because the deceased did not, with full knowledge of the issues, impliedly authorise the conflict by appointing his mother as his executor under a Will.

(d) ‘An administrator of an intestate estate has a duty to apply for payment of the superannuation funds to the estate. The administrator has no proprietary right to the funds but has standing to compel the trustees of the fund to exercise their discretion to pay out the funds.’ 23

(e) If the mother did not have a person conflict, she would have as administrator applied for the superannuation death benefit to be paid to the estate.

8.5 This case has received a significant amount of attention since it was handed down on 16 May 2014 even though it did not change the established law in this area.

8.6 Despite the fact that the case did not change the law, I believe that it will have significant practical implications. In particular, I am concerned that this case may result in the following:

(a) Where the superannuation benefits are in a retail or industry superannuation fund, the trustee of the fund will, out of an abundance of caution, refuse to pay or not even consider paying the superannuation death benefit personally to a person who is also the executor or administrator of the estate.

If this position is adopted by the trustees of retail and industry superannuation funds, I am concerned that:

(i) where the surviving spouse is also the executor of the estate (as is usually the case), the superannuation fund trustee will not pay the superannuation death benefit to the surviving spouse as a pension which will potentially result in additional tax being payable; and

(ii) the estate being the default payment option for the superannuation death benefit, even though this may not be the desired outcome. 24

(b) An increase in the number of challenges to the trustee’s exercise of discretion where the beneficiary of the superannuation death benefit is also the executor or in the case of an SMSF, the controller of the SMSF.

8.7 As a result, we should be cautious where a person who may wish to be considered as a beneficiary of superannuation benefits is involved with making the decision, or may be the executor or administrator of the estate.

8.8 To overcome this issue, there are a variety of steps we can take to ensure the benefits are paid as intended despite the fact that there may be a conflict.

(a) Appoint someone other than the intended recipient of the superannuation death benefit as the executor. This can be quite difficult as it is common for the intended recipient of the superannuation death benefit to be the obvious choice as the executor (for example, the surviving spouse).

However, where there is another suitable person to act as the executor, this is a potential option as it removes the conflict completely.

23 [2014] QSC 99 at [71]
24 See the discussion at paragraph 5.3
(b) Remove the superannuation trustee’s discretion and force the superannuation death benefit payment to the intended recipient by way of binding nomination, reversionary pension or specific trust deed provision.

Although this option deals with the conflict issue, it does not address the usual concerns that arise when making a decision on how the superannuation death benefit is payable in advance of the death of the member (see the discussion at paragraph 3).

(c) Provide the trustee with a direction or non-binding nomination which clearly authorises the trustee of the superannuation fund to pay the superannuation death benefit to a person in a conflict position.

Although this nomination will not be binding on the trustee, it may be sufficient to remove the concern regarding the potential conflict.

(d) Include a clause in the Will that expressly authorises the executor to also pay or apply to receive the superannuation death benefit personally. This is my preferred option.

However, it will be critical that this clause does not authorise every conflict as this could have unintended consequences – for example, you do not want to authorise one child to apply for the superannuation benefits where it is intended to be split between all the deceased’s children equally. As a result, where I have included a conflict clause in a Will, it is very specific and expressly authorises a conflict in a limited situation.

9. CONCLUSION

Although this paper does not address all the issues with superannuation in an estate planning context, hopefully it provides a useful insight into the breadth of issues that must be considered when you are engaged to prepare even the simplest Will for a client.

As advisors we must ensure that we have prudently considered the issues relating to the superannuation death benefit in drafting a Will, including ensuring the Will is structure correctly to deal with all the possible alternatives that may arise.

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This paper is only intended as a general overview of issues relevant to the topic and is not legal advice. If there are any matters you would like us to advise you on in relation to this paper, please let us know.