

Binding Death Benefit Nominations

– Qs and As



Since 1999, when the superannuation rules were amended to permit members of superannuation funds to make binding death benefit nominations (**BDBN**), there has been some ongoing debate regarding the relevance of the changes to self managed superannuation funds (**SMSF**). This information brochure answers key questions in this regard, including whether *non-lapsing* nominations can be made and whether a death benefit paid in accordance with a BDBN can be clawed back into the deceased's estate.

Q. What is a BDBN?

A. A BDBN is a notice given by a super fund member to the trustee of their super fund *requiring* a death benefit to be paid to the member's nominated *dependant(s)* and/or *legal personal representative* (see *Who can be nominated in a BDBN?*, below).

Without a valid BDBN in place, the super fund trustee will, for better or worse, determine which one or more of the member's dependants and/or legal personal representative receive the death benefit.

Q. Who can be nominated in a BDBN?

A. A deceased member's death benefits can generally only be paid to one or more of their *dependants* and/or their *legal personal representative*. Hence, the only people who can be nominated in a BDBN are one or more of their dependants and/or their legal personal representative.

A person's *dependants* include their **spouse**, any **child**, any person with whom they have an **interdependency relationship** and any person who is financially dependent on them. **Spouse** includes same-sex de facto spouse and **child** includes adopted child, stepchild, ex-nuptial child and child of the person's spouse. Two persons have an **interdependency relationship** if they have a close personal relationship and either:

- they live together and one or each of them provides the other with financial and domestic support and personal care; or
- they do not satisfy the other requirements of an interdependency relationship because either or both of them suffer from a physical, intellectual or psychiatric disability or they are temporarily living apart, eg because one of them is temporarily living overseas.

A deceased person's *legal personal representative* means the executor of their will or administrator of their estate.

Q. What are the technical requirements for a valid BDBN?

A. Subject to the comments at *Do the same BDBN rules govern SMSFs below?*, for a BDBN to be valid:

- the trustee of the super fund must give to the member information that the member needs to understand their right to require the trustee to provide the benefits;
- the governing rules of the fund must permit a member to require the trustee to pay a death benefit to the member's nominated dependant(s) and/or legal personal representative;
- the person, or each of the persons, nominated must be a dependant or the legal personal representative of the member;
- the proportion of the benefit that will be paid to that person, or to each of those persons, must be certain or readily ascertainable from the notice;
- it must be in writing;
- it must be signed and dated by the member in the presence of two adult witnesses, neither of whom is mentioned in it; and
- it must contain a declaration, signed and dated by the witnesses, stating that it was signed by the member in their presence.

Q. How long can a BDBN remain in force?

A. Subject to the comments at *Do the same BDBN rules govern SMSFs?*, below, a BDBN will expire:

- at the end of three years after the day it was first signed, or last confirmed or amended by the member; or
- if the governing rules of the fund fix a shorter period, at the end of that period.

Irrespective of the longevity of the BDBN in question, because members' circumstances change, we recommend that those with BDBNs be given the opportunity to confirm, amend or revoke their nomination at least annually.

Q. Do the same BDBN rules govern SMSFs?

A. On reading of the relevant legislation (sub-sections 59(1) and 59(1A) of the *Superannuation Industry (Supervision) Act 1993* (Cth)), the BDBN rules that govern *large* super funds need not govern SMSFs and the extent to which they do depends on the precise wording of the governing rules. This question must, therefore, be answered on a case by case basis.

While sub-section 59(1) generally prohibits the exercise of discretion by a person other than a trustee of the fund:

- the prohibition expressly does not apply to SMSFs; and
- sub-section 59(1A) provides an express exemption from the prohibition for BDBNs to be made in accordance with regulation 6.17A of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (**SISR**) (the requirements of which are detailed in "*What are the technical requirements for a valid BDBN?*", above).

So, why the uncertainty?

The Regulator's Perspective

While it is reassuring the ATO agrees "that the governing rules of an SMSF may permit members to make death benefit nominations that are binding on the trustee, whether or not in circumstances that accord with the rules in regulation 6.17A" (refer *Self Managed Superannuation Funds Determination SMSFD 2008/3* dated 17 December 2008), *Self Managed Superannuation Funds Determinations* are not legally binding on the ATO or anybody else and the courts have provided precious little guidance to date.

Case Law

In the recent Queensland Supreme Court case of *Donovan v Donovan* [2009] QSC 26, Justice Fryberg was given the opportunity to consider whether sub-section 59(1A) and regulation 6.17A apply to SMSFs. Unfortunately, he declined to do so.

In *Donovan*, the deed provided that in respect of a payment of a death benefit:

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

and Justice Fryberg was of the opinion that:

it is quite plain that the intent of the deed is to require the nomination to be in the form described in regulation 6.17A(6).

Also, that:

It is very easy for trustees and members to make a mistake about the requirements applicable in their particular case. It is very understandable that a deed should specify a requirement in effect to comply with the form described in regulation 6.17A(6) out of an abundance of caution. The alternative would be to require the trustees or the member to take legal advice about the answer to the first question posed to me (whether sub-section 59(1A) and regulation 6.17A apply to SMSFs), and to run the risk that their advice might turn out to be incorrect. Such an approach is uncommercial and unlikely.

Conclusion

Trustees and members of SMSFs need to take extreme care to clarify in their governing rules precisely the extent to which the BDBN rules that govern *large* super funds are meant to govern their fund, including, for example, in the context of how long a BDBN can remain in force, whether that be for up to three years or even longer; indefinitely, perhaps.

Q. What level of detail can a BDBN contain?

A. Many pro-forma BDBNs offer members the opportunity to do no more than nominate one or more of their *dependants* and/or their *legal personal representative* and the proportion of the death benefit that will be paid to each of those persons, whereas in our opinion, they can do so much more. A more sophisticated BDBN can, for example:

- identify specific assets to be paid to particular beneficiaries;
- specify the manner in which the benefit will be paid, eg a lump sum (cash or *in specie*) or pension; and/or
- include alternative beneficiaries in case one of the primary beneficiaries pre-deceases the BDBN-holder.

Q. What are some of the advantages of a BDBN?

A. Advantages of a BDBN include:

- certainty; ie that death benefits will be paid in accordance with the deceased member's wishes; and
- less likelihood of a successful challenge by a disgruntled beneficiary.

Q. What are some of the disadvantages of a BDBN?

A. Disadvantages of a BDBN include:

- that the member must remember to review their BDBN regularly;
- the possibility that the member's circumstances change and they die:
 - with an inappropriate BDBN in place; or
 - without a valid BDBN in place;
- that the trustee will be bound to comply with a valid BDBN, whether it is still appropriate (including equitable and tax-effective) or not;
- if the member loses capacity, their legal personal representative may not be able to confirm, amend or revoke their nomination.

Q. When might a BDBN be appropriate?

A. Examples of situations in which a member might make a BDBN include the following:

- A member has two children, only one of whom is a trustee of his SMSF. He makes a BDBN because he wants each child to receive an equal share of any death benefit. Readers familiar with the New South Wales Supreme Court case of *Katz v Grossman* [2005] NSWSC 934 will likely appreciate that the making of a BDBN in circumstances similar to these may well have kept Mr Katz's children out of court.
- A member is married for the second time. She makes a BDBN because she wants her current husband to receive any death benefit. Were any death benefit to be paid to her legal personal representative, it would form part of her estate and her Will could be challenged or contested by the children of her first marriage.
- A member has three adult children, one of whom is experiencing marital difficulties for the second time, another of whom is a recovering alcoholic and the other of whom is facing the prospect of bankruptcy. He makes a BDBN because he wants any death benefit to be paid to his legal personal representative who will hold his estate in a series of testamentary trusts.

Q. Can all super fund members make a BDBN?

A. No. Super fund members can only make BDBNs if the governing rules of their fund expressly permit them to do so.

While super fund trustees are under no obligation to offer members the opportunity to make BDBNs, if the governing rules do not currently permit members to make BDBNs and the trustee wants to give them that opportunity, the trustee can generally amend the governing rules to permit them to do so.

Q. Can the holder of an enduring power of attorney make a BDBN?

A. A BDBN is not a testamentary instrument. It is, therefore, at least arguable that the holder of an enduring power of attorney can make, confirm, amend or revoke a BDBN for the person on whose behalf they hold the enduring power of attorney, particularly if there is an express power in the enduring power of attorney authorising them to do so.

Q. Is a death benefit nomination binding if it nominates someone that it shouldn't?

A. No. The ATO confirms in *Self Managed Superannuation Funds Determination SMSFD 2008/3* that a death benefit nomination is not binding on a trustee to the extent that it nominates a person who cannot receive a benefit in accordance with the super rules, generally one or more of the member's dependants and/or their legal personal representative.

Note that with effect from 1 July 2007, regulation 6.21 of the SISR further restricts the persons to whom a trustee can pay a death benefit in the form of a pension to a person who is a dependant of the deceased member, and in the case of a child of the member:

- is less than 18 years of age; or
- being 18 or more years of age:
 - is financially dependent on the member and less than 25 years of age; or
 - has a prescribed kind of disability,

so trustees and members should revisit any pre-1 July 2007 BDBNs that nominate adult children to receive pensions.

Note also that the ATO would appear to be of the view that to the extent that the payment of a benefit would contravene the super rules, the payment becomes subject to the discretion of the SMSF trustee.

Q. Will a BDBN override reversionary pension documentation?

A. Generally will not, though the answer may differ depending on the precise wording of the trust deed, the pension paperwork and the BDBN in question. Clearly, inconsistency between pension paperwork and a BDBN should be avoided!

Q. Can a death benefit paid in accordance with a BDBN be clawed back?

A. A death benefit paid in accordance with a valid BDBN cannot currently be clawed back into the deceased's estate in any State or Territory except New South Wales.

In New South Wales, on the other hand, the courts may have power to claw back into the deceased's estate death benefits paid in accordance with a valid BDBN, but only in limited circumstances.

Topdocs can advise in relation to and can draft BDBNs. Please contact us on 1300 659 242 with any queries that you may have in relation to BDBNs or super or estate planning documentation more generally.