

SUPERANNUATION DEATH BENEFITS - A VITAL COMPONENT OF ESTATE PLANNING

Contrary to a common misunderstanding, an individual's Superannuation Death Benefits are not directed by their Will. It is vital that an individual's estate planning considers the special rules applicable to assets they hold in superannuation, as well as their assets outside of superannuation.

This article looks at the rules covering the payment of superannuation death benefits and how control of the payment decisions may be implemented.

What is Estate Planning?

Estate planning can be described as the structuring of an individual's financial affairs so that, on their eventual death, the person's potential (and preferred) beneficiaries are cared for financially in the most efficient and cost effective way possible.

With the assets an individual holds in superannuation forming a significant component of their wealth, particularly when insurance benefits are added, consideration as to how a person's superannuation will be treated on death forms an important part of the estate planning process.

Superannuation Death Benefits - What are they?

Superannuation death benefits are basically the payment to a person from a superannuation fund because the deceased

person was a member of that superannuation fund.

The benefits can be paid either from the accumulation account of a deceased member, or from any pension account held for them.

Specific tax concessions, which may not be available in other circumstances, can apply to the payment of superannuation death benefits.

To whom can the benefits be paid?

A superannuation death benefit can be paid, in the first instance, to either the legal personal representative (LPR) of the deceased, or any person who is classified as a dependant under the Superannuation Industry (Supervision) Act 1993 ('SIS Act').

If neither a LPR nor any other such dependant exists at the time of the member's death, a broader category of recipients may be considered.

It is important to note that there are a number of different definitions of 'dependant' which apply in the superannuation

environment, the two main definitions being:

- dependants under the SIS Act, generally referred to as 'SIS dependants'; and
- dependants under the Income Tax Assessment Act 1997 ('Tax Act'), generally referred to as 'tax dependants'.

A person who is classified as a SIS dependant may not meet the definition of a tax dependant meaning that, although they are entitled to receive a superannuation death benefit, it may be subject to tax. This can particularly impact the children of the deceased.

What is an LPR?

The term 'legal personal representative' covers a range of scenarios for people at different stages of their lives but, for a deceased person, it refers to the executor of their Will, or administrator of their estate.

Any superannuation death benefit payment to the LPR will therefore form part of the deceased person's estate.

Current as at 3 July 2014.

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Who can be a SIS dependant?

The SIS Act defines a dependant of a deceased member of a superannuation fund as any of:

- the spouse (married or de-facto, and including those in a same-sex relationship provided the relationship has been registered) – there can be more than 1 spouse at a given time;
- any child of the deceased; and
- any person with whom the deceased had an ‘interdependency relationship’.

As the SIS dependant definition is an ‘inclusive’ definition, financial dependency may also meet the definition, in addition to those categories specifically listed above.

What defines a ‘child’?

The range of individuals who may be classified as a child can be quite broad, including:

- adopted, step or ex-nuptial children;
- children of a person’s spouse; and
- children under the broader context of the Family Law Act.

The tax definition of dependent for death benefit purposes limits dependent children to those under 18 years of age.

The ATO, in an Interpretative Decision, ID 2011/77, considered the issue of ‘stepchild’ in the context of the divorce of a child’s natural parent and the step-parent.

The ATO’s decision was that the “relationship of stepchild to step-parent is severed when the marriage between the natural parent and the step-parent ends ...”. That would apply either:

- on the death of the natural parent; or
- on the divorce of the natural parent from the step-parent.

The term ‘stepchild’ only applies, as detailed in the ATO decision, in relation to individuals who are legally married. If the couple was in a de-facto relationship, the definition ‘children of a person’s spouse’ would apply (with the same result under the definition, if the relationship ended).

In either of the scenarios outlined above, the stepchild or stepchildren would need to demonstrate some other dependency, such as interdependency or financial dependency, to meet the definition of SIS dependency.

What is required to confirm an interdependency relationship?

Section 10A of the SIS Act states that two persons (whether or not related by family) have an **interdependency relationship** if:

- (a) they have a close personal relationship; **and**
- (b) they live together; **and**
- (c) one or each of them provides the other with financial support; **and**
- (d) one or each of them provides the other with domestic support and personal care.

The only exception permitted to the requirements above relates to the second requirement – that they are living together. If the individuals are **unable** to live together because of a disability, but meet the other requirements, they will be considered to be in an interdependency relationship.

Can adult children have an interdependency relationship with a parent?

The Superannuation Complaints Tribunal has considered this question, and has determined that it is possible for an interdependency relationship to exist between a parent and their adult child.

This can have significant tax and estate planning consequences when, for example, an individual

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resides in an interdependency relationship with one of a number of the person's adult children.

Who can be a financial dependant?

There is no limitation to the range of people who may be financial dependants. As the term 'financial dependant' is not defined in either the SIS Act or the SIS Regulations, the fund trustee has the responsibility of determining whether a person was financially dependent on the deceased member at the time of their death, in accordance with any instructions contained in the governing rules, such as the trust deed, of the fund.

The Australian Prudential Regulation Authority (APRA) has stated that **partial** financial dependency is sufficient to meet the definition of 'dependant' for the purposes of the SIS Act and SIS Regulations.

What if there are no SIS dependants surviving the member?

That situation may occur, for example, following the death of a young person who was not in a relationship (as a couple), had no children, had not made a Will and had no assets other than superannuation savings.

In that instance, there is unlikely to be any need for a relative to apply for letters of administration, meaning there

will be no LPR to whom the trustee could pay the superannuation death benefit.

So long as the governing rules of the fund permit, the trustee is able to pay the death benefit to another person, such as a parent of the member.

How may the benefits be paid?

Superannuation death benefits can be paid as a lump sum or, in limited circumstances, as a pension. The limitations in regards to the payment of a pension relate to children of the deceased member.

A pension may only be paid to a child if the child:

- is under 18 years of age; or
- is under 25 years of age **and** is financially dependent on the member; or
- has a disability.

If the payment is to be made in the form of a lump sum, certain timing rules may apply for the payment to be treated as a superannuation death benefit.

When the payment follows the commutation of a pension, including a pension which reverted following the death of a member, it must be paid before the **later** of:

- 6 months after the date of death; and

- 3 months after the grant of probate or letters of administration.

A lump sum payment made from the member's accumulation account, regardless of the timing of the payment, will be a superannuation death benefit.

Who decides who will receive the benefits and in what form?

The trustee is considered by many to be the main decider as to the type and amount of superannuation death benefits payable, and the recipient or recipients.

However, in many SMSFs in particular, there is a range of options available to the member, or a trusted adviser, to control the amount and type of superannuation death benefits paid following the death of that member.

Those options include:

- **Automatic Reversion of Pensions**, in which the pension payable to a member automatically becomes payable to another person (nominated previously by the member) on the death of the member, provided the nominated person is entitled to receive a pension under SIS rules;
- **Non-Binding Death Benefit Nominations** which are, in effect, suggestions to the

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trustee as to who the member wishes payment be made, with the ultimate decision left to the discretion of the trustee;

- **Non-lapsing Binding Death Benefit Nominations**, which remove any discretion from the trustee so long as the nominated recipients are SIS dependants at the time of death of the member.

The Topdocs binding death benefit nominations can be structured to include a direction as to specific assets and/or specific proportions to pass to intended beneficiaries and, in the event of those nominated recipients either not surviving or not being entitled to receive the benefit, a secondary nomination is available.

- **Binding Death Benefit Rule**, effectively a rule written into the trust deed by the trustee at the request of a member, which sets out the conditions regarding the payment of the benefit at the time of the death of the member.

The Topdocs SMSF trust deed empowers the trustee to accept a request from a member to write a binding death benefit rule, and to amend the deed by writing the rule.

- **Death Benefit Guardian**, where a member has the option to appoint a Death Benefit Guardian, which prevents the trustee from undertaking certain actions without the written consent of the Guardian.

If appointed, a Death Benefit Guardian's consent would be required by the trustee prior to making superannuation death benefit payments, where neither a reversionary pension nor a valid binding death benefit nomination is in place.

The Topdocs SMSF trust deed provides for the appointment by each member of a Death Benefit Guardian, should they wish to do so.

What benefit can a Death Benefit Guardian provide?

In a close family, the need to appoint a Death Benefit Guardian may not seem to be an issue. However, let us consider the case of *Katz v Grossman* where, briefly, benefits which were assumed to pass equally to the 2 children of the deceased member were actually paid, at the discretion of the trustees, all to the one child who also happened to be a trustee of the fund (with her husband as the other trustee).

Had either a trusted friend, or even the other child, been

appointed as a Death Benefit Guardian, the trustees could not have made the payment without the consent of the Death Benefit Guardian. In the case of *Katz v Grossman*, it is more likely that the intended equal distribution would have occurred, because of the oversight of the Death Benefit Guardian.

Planning for the payment of superannuation death benefits

The Topdocs SMSF trust deed and related documentation can assist in providing a degree of certainty to the estate planning process, through enabling members to control the distribution of their benefits in the event of their death

More information

Should you have any queries, or require more information, please contact the team at Topdocs on 1300 659 242