

BDBNS

- LET'S TAKE A STEP BACK

Binding Death Benefit Nominations, or BDBNs, have been part of the superannuation landscape for quite some time. But not all have worked as intended.

With an increasing amount of case law illustrating what can go wrong with BDBNs, Michael Harkin, National Manager for Training and Advice at Topdocs, takes a look back to review the evolution of BDBNs and in doing so, highlights matters which trustees and their advisers must consider when having BDBNs prepared.

SIS provisions

Section 59 of the SIS Act permits discretion over death benefit payments to be exercised by another person, where:

- the nomination of death benefit recipients is in accordance with the SIS Act (s 59(1A)); or
- the trustee consents to the exercise of that discretion (s 59(1)(a)).

Regulation 6.17A of the SIS Regs contains procedural details, such as information the trustee needs to provide, signing and witnessing the document and limitations on who may be nominated as beneficiaries.

Impact on SMSFs

In SMSFD 2008/3, the ATO confirmed that SIS Act s 59 (and SIS Reg 6.17A) do not apply to SMSFs.

That means “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 of the SISR.”

However, as covered later, some SMSF deeds link the ability of members to provide death benefit instructions to the provisions of the SIS Act.

The impact of such links in a trust deed is one of the reasons why estate planning can go wrong, through lack of understanding of requirements in the deed.

What needs to be done?

Firstly, let's consider the steps in creating BDBNs, to ensure the instructions of the deceased can be put into effect.

Important considerations to ensure validity of the BDBN are highlighted in the section on case law.

Trust Deed

As with many SMSF actions, an important question needs to be asked - ‘What does the trust deed permit/require?’

The correct interpretation of those provisions is a vital component of ensuring validity of a BDBN.

Completion

Ensuring a BDBN is correctly completed, in accordance with the terms of the deed, is sometimes overlooked.

Examples of poor completion include:

- percentage allocations of benefits exceed 100%;
- nominated beneficiary is not a SIS dependant; and
- witnesses are listed as beneficiaries.

Witnessing

The witnessing requirements should be detailed in the trust deed.

Witnessing of a BDBN not in accordance with the rules of the deed is likely to invalidate the BDBN.

Beneficiaries

Nomination of a beneficiary who is not a SIS dependant may invalidate the BDBN.

For example, the nomination of a foster daughter may fail, as they would not meet the definition of ‘child’ under SIS. However, if they were:

- a financial dependant of the deceased; or
- in an interdependency relationship with the deceased;

at the time of death, they would be a SIS dependant and could receive a benefit under the BDBN.

Process to instruct Trustee

Again, the SMSF trust deed should contain instructions of the process to be followed when, and how, the trustee receives the BDBN prepared by the member.

Current as at 28 September 2015.

Please note this article is for information purposes only and does not constitute legal or financial advice.

BDBNS

- LET'S TAKE A STEP BACK

An example of how this can cause confusion will be outlined when we consider case law.

Review

Once the BDBN has been completed, a final review of the document should be undertaken, checking that all requirements have been attended to correctly and will not result in an invalid BDBN.

What has gone wrong

Since the introduction of the SIS Act, many BDBNs have successfully directed death benefits of deceased members to those nominated to receive benefits.

However, not all have gone according to plan, as a growing list of legal cases indicates. Additionally, it could be expected that, for each case which reaches court, a number of disputes:

- will be settled 'out of court'; or
- may be dropped because of the cost of taking action.

From a planning perspective, much can be learned from evolving case law.

A summary of a number of relevant cases are detailed below:

Katz v Grossman

Basically, the first case regarding SMSF death benefits, this case highlighted the need for a BDBN.

Mr & Mrs Katz were trustees of their SMSF:

- following the death of Mrs Katz, their daughter, Linda Grossman, was appointed as the 2nd trustee;

- Mr Katz passed away (in his Will, he appointed his daughter and son as executors, leaving his estate to both equally);
- Linda appointed her husband as the second trustee;
- Mr Katz had not left a BDBN, so the trustees distributed all benefits to Linda; and
- her brother took action to claim a share of the benefit.

The action failed, as the trustees were not in breach of the provisions of the trust deed.

Had Mr Katz left a valid BDBN directing the benefits equally to both children, Mr & Mrs Grossman could not have made the decision they ultimately made.

Donovan v Donovan

In that case, the SMSF trust deed stipulated that a BDBN be made 'in the form required to satisfy the Statutory Requirements'.

The fact that the BDBN was not in accordance with the SIS requirements was a reason the decision of the trustee (contrary to the nomination), was not overturned by the Court.

In other words, the BDBN failed because the trust deed linked it to the requirements in SIS. As the BDBN was not prepared in accordance with those requirements, it failed.

Ioppolo v Conti

Mr & Mrs Conti were trustees of their SMSF:

- Mrs Conti, in her Will, appointed her daughters as executrices and directed:

- her superannuation to her daughters; and
 - that Mr Conti receive no superannuation benefits.
- Mrs Conti passed away, leaving Mr Conti as the surviving trustee;
- Mr Conti:
- appointed a corporate trustee - he was sole director; and
 - distributed Mrs Conti's benefits to himself.

In that case, the daughters launched action on 2 fronts, that:

- they be appointed as trustees of the SMSF (presumably to stop Mr Conti from acting as he did); and
- Mr Conti had not acted in a bona fide manner (a requirement in the trust deed) in providing the benefits to himself.

The action by Mrs Conti's daughters failed on both matters, the Court ruling Mr Conti had acted in a bona fide manner and in accordance with the trust deed.

Wooster v Morris

Mr & Mrs Morris were trustees of their SMSF:

- Mr Morris made a BDBN directing his superannuation to his daughters;
- the SMSF trust deed directed that the BDBN be 'given' to the trustees;
- as the BDBN had not formally been presented to Mrs Morris, she sought legal advice as to the validity and was advised there was a chance it may be invalid; and

Current as at 28 September 2015.

Please note this article is for information purposes only and does not constitute legal or financial advice.

BDBNS

- LET'S TAKE A STEP BACK

- Mrs Morris paid the benefits to herself.

A Court appointed Referee determined that the BDBN was valid and binding, so the superannuation death benefits of the deceased were to be paid to the daughters.

McIntosh v McIntosh

A non-SMSF case, another with no BDBN, Mr & Mrs McIntosh had been divorced and, it is understood, Mrs McIntosh had been sole parent to their son for many years.

The son passed away, leaving no Will but a non-binding death benefit nomination over his public offer superannuation benefits.

Subsequently:

- Mrs McIntosh applied for a grant of letters of administration of her son's estate;
- she applied to the fund for his superannuation benefits;
- the fund paid the benefits to Mrs McIntosh as she and her son were in an interdependent relationship; and
- Mr McIntosh commenced action to direct that the benefits received by Mrs McIntosh should have been applied to the estate and, therefore, divided between Mr & Mrs McIntosh under the rules of intestacy.

The Court directed that Mrs McIntosh, as the legal personal representative, had a higher duty to the estate than herself and, therefore, was required to pay the benefits to the estate.

Had the son left a valid BDBN, the situation would have been different. Mrs McIntosh would have received the benefits under the BDBN.

Munro v Munro

Another case with an ineffective BDBN:

- Mr Munro left a BDBN, directing his benefits to be paid to the 'trustee of deceased estate';
- however, the trust deed permitted a BDBN to direct benefits be paid to certain beneficiaries or to the 'legal personal representative'.

The Court determined that the trustee of the estate is not a legal personal representative, so the nomination was invalid.

Stock v N.M. Superannuation

This, the most recent of the relevant cases, is not related to an SMSF, but to a Federal Court appeal against a Superannuation Complaints Tribunal (SCT) decision.

The executors (Stock and others) of the Will of the late Mr David Mandie objected to payment of superannuation death benefits. Mr Mandie:

- directed all of his estate to his daughter, under his Will;
- directed that, as he had reached a financial settlement with his two sons some years prior, where they agreed they had no further interest in his estate, no benefits were to pass to them;
- had not left a BDBN, and the trustee resolved to divide the benefits equally between his three children.

The decision of the trustee to divide the superannuation equally caused the appeals to the SCT and, ultimately, the Federal Court.

The appeals were unsuccessful, again highlighting the need for effective estate planning to consider a BDBN for superannuation benefits.

Overcoming problems

The most common theme from the cases detailed above is the incorrect assumption that the Will of an individual can direct the distribution of superannuation benefits.

The other theme which was dealt with in some cases was the invalidity of BDBNs, whether through lapsing due to time, linking to the SIS provisions, or incorrect nominations.

Some ways potential problems may be overcome, include:

- ensuring the trust deed of the SMSF is current and any BDBN is prepared in accordance with provisions contained in that deed;
- when updating the trust deed, ensuring the provisions of the new deed provide for a BDBN prepared under the earlier deed;
- using a document provider which applies industry standard terms, rather than introducing different names for documents which can lead to confusion;
- ensuring the trust deed provides directions as to which document will take precedence in the event of any potential conflict between a BDBN and other death benefit documents, particularly a pension reversion

Current as at 28 September 2015.

Please note this article is for information purposes only and does not constitute legal or financial advice.

BDBNS - LET'S TAKE A STEP BACK

nomination and a death benefit rule.

Advisers and members should also consider the viability of appointing a Death Benefit Guardian - someone who must approve the decision of the SMSF trustee to pay benefits in the event that there is no valid BDBN or other document directing the payment of death benefits of a member.

Conclusion

As case law indicates, an increasing number of disputes have reached court for a decision. With the increase in superannuation balances, together with increases in blended family scenarios, further action is likely in instances where effective planning has not been undertaken, with BDBNs at the forefront of that planning.