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His current role focuses on providing technical, strategy and lead generation advice to risk specialist advisers in areas such as estate and business succession, business structures, superannuation and He regularly conducts workshops for advisers and speaks at industry conventions.

MAKING THE RIGHT SUPER BENEFICIARY NOMINATION

Jon de Fries

There are various types of super beneficiary nominations available that fund members can make. It's an important area of financial advice, considering a member's death benefit will often be considerably boosted by insurance proceeds and be their largest financial asset.

This article will take a look at the pros and cons of the various types of nominations – particularly binding nominations versus non-binding nominations.

Since the introduction of binding nominations to the super legislation in 1999, the prevailing view in our industry has often been that binding nominations are best, but this is not always the case.

Note: this article is not intended to be an in depth analysis of taxation issues in relation to super death benefits.

Binding Nominations

When a super fund member makes a valid binding nomination to their fund trustee, the trustee is bound to pay that member's nominated beneficiary – the trustee cannot exercise discretion or investigate other potential beneficiaries. In this context, the other alternative is a binding nomination to multiple beneficiaries, typically each with nominated percentages of the death benefit.

The super legislation only allows five types of beneficiaries in relation to valid dependant beneficiary nominations:

- The member's spouse – married and de facto (including same sex). It's possible to have more than one spouse – for example, a person who remains married but is separated from their spouse and has entered a new de facto relationship;
- The member's children – both minors and adult, including adopted and ex-nuptial, but not always step children ;

- A person in an interdependency relationship with the member – the over-riding criteria is that the person was (unless illness-separated) living with – and had a 'close personal relationship with – the deceased at time of death.'
- A person financially dependent on the member. While we are discussing the super context, it should be noted that for tax purposes, the ATO sets a high bar – their view is that financial dependence is 'where a person is wholly or substantially maintained by another person' . This is often interpreted as at least 50% support in relation to the dependant's necessary living requirements; and
- The member's legal personal representative (i.e. the estate) - the person's executor/s if the person has died with a valid Will (i.e. The Supreme Court has given Grant of Probate) or the person's Administrator/s if the person has died without a valid Will (i.e. died intestate and Letters of Administration have been granted by the Supreme Court).

Of course, any payment to the estate under any type of nomination opens up the possibility of eligible people challenging to get some or all of those proceeds – either on the grounds that they have not been adequately provided for (the list of eligible people differs from this list and from State to State) or on the grounds that the deceased did not have capacity when they signed the Will (assuming there was a Will).

Additionally, in NSW, a death benefit paid to a beneficiary could be characterised as a 'relevant property transaction' in certain circumstances, and form part of the deceased member's 'Notional Estate'

The fund trustee may pay death benefits to another individual if they have 'not, after making reasonable enquiries, found either a legal personal representative, or a dependant' . For example, where a young single person has died, death benefits are sometimes paid to their parents.

Binding Nominations - lapsing

Generally trustees have discretion over various matters in the running of the fund in accordance with its governing rules, including whom a death benefit is paid to – that is, members cannot direct trustees. An exception to this general rule is Self-Managed Super Funds (SMSFs) as, with few exceptions, the members are the trustees.

As mentioned, an amendment to this general rule was introduced in 1999 to allow non-SMSF members to direct trustees as to who to pay a death benefit to (within the above list), removing their discretion if the trustee chose to allow this in their governing rules. This nomination must be given to the trustee on a notice signed by the member with the signature witnessed by two people aged 18 or over other than the nominated beneficiaries. Under this amendment, these notices lapse within three years.

Binding Nominations – non-lapsing

Since the introduction of this measure, legal personnel working for various fund managers have examined the general rule that trustees cannot be directed and used the provision in SISA that the trustee can be bound if the trustee gives consent to pave the way for non-lapsing binding nominations.

The main impetus for this innovation was the onerous task of administering lapsing binding nominations, including the necessity of sending out reminder letters every three years to members to renew or update their nominations, the failure of members to return these (with the nomination reverting to non-binding), and administering the responses. Additionally, funds who offered non-lapsing binding nominations could market greater succession planning certainty to financial advisers and members.

Non-lapsing binding nominations also have a significant advantage in an era of rising mental health issues, where aging members are increasingly developing conditions such as dementia and losing capacity to sign documents.

So non-lapsing binding nominations are appropriate when certainty that a nominated beneficiary, beneficiaries and/ or the estate will be paid is paramount to a client. However, the trade-off is a loss of flexibility that might be preferable given it will generally be uncertain what will ultimately be best for beneficiaries (when they are to receive the death proceeds) at the time of nominating.

One important point to note is that a binding nomination (both lapsing and non-lapsing) does not bind the beneficiary/s as to the form of the death benefit. They can generally choose (at the time of death) whether they take the benefit as a lump sum, pension or combination of these, bearing in mind that in relation to the five alternative valid nominations in the above list, pensions cannot be paid to children 25 or above (unless they are disabled) or to the deceased's estate.

Another issue to bear in mind is that, anecdotally, many fund managers find it difficult administratively to pay multiple pensions from a deceased member's account. This may give SMSFs the edge as the preferred vehicle if (for example), a client has a spouse and young children and in the event of death wishes to make use of multiple tax-free thresholds and low marginal tax rates.

Binding Nominations – non-lapsing in SMSFs?

The ATO released an SMSF Determination in 2010, which contained the view that all valid binding nominations made to an SMSF trustee were non-lapsing binding. There are some differing legal opinions on this which arise from a perceived contradiction within the relevant section in the legislation (see footnote 1). In other words there is a school of thought that SMSF members who desire binding nominations should adhere to the three year renewal process.

The ATO in the Determination state they do 'not agree with this interpretation'.

SMSF governing rules generally (in the absence of binding nominations received under their provisions) grant the trustee discretion as to which beneficiary/s the death benefit is paid to. This discretion can, of course, lead to family stoushes – such as the well-known Katz v Grossman case [2005] NSWSC 934.

It should be remembered that disgruntled SMSF members do not have access to the Superannuation Complaints Tribunals (SCT), which is a statutory, free body established about 20 years ago where non-SMSF members can lodge complaints against superannuation trustees' discretionary decisions (mainly in relation to the payment or non-payment of death and disability benefits).

Non-binding nominations

Many legal and other advisers promote the value of non-binding nominations. These can be useful where:

- It's desirable to have flexibility at the time of death as to who is paid. The client may wish to retain flexibility to decide how much of the benefit is to be paid the estate (for example, to be placed into a testamentary trust to protect their beneficiaries), how their beneficiary/s take as a pension and how much is paid as a lump sum (to clear debts and pay immediate expenses);
- The multiple pension strategy (mentioned above) is to be implemented. One version of this strategy is to give younger children larger pension accounts and older children smaller accounts in order to maximise the total years of tax effective income. To optimise this, the calculations as to how much is allocated into each account would ideally be done on death.
- Beneficiaries' circumstances are expected to change. For example, at the time of planning, a client's child is a dependant for tax purposes (and can receive super tax-free and/ or as a pension), but in the not too dis-



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tant future this may change.

The main issues with non-binding nominations are that:

- Trustees in retail and other large funds will generally be obliged to follow a procedure whereby they identify and contact other valid beneficiaries to confirm they are happy with the deceased member's nomination;
- Disgruntled (valid) beneficiaries who feel they have not received their fair share of a super death benefit may complain to the SCT. Examples would be children from a former marriage, siblings fighting each other or even spouses who – though separated – remain legally married to the deceased.

Summary

Super death benefits advice is a crucial part of financial planning. At a high level, advice should cover:

- The level of insurance in super
- Whether super should be directed away from – or towards – a client's estate (or combination of these)
- Whether the flexibility of a non-binding nomination or the certainty of a binding nomination is suitable for a client
- What combination of pensions and lump sums may be appropriate for beneficiaries. **FS**



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