

SMSF Estate Planning

A matter of control and BDBNs

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“You never really know someone until you share an inheritance with them.”

Mark Twain



Agenda

- What happens to member benefits on death?
- Why is it important to make a BDBN?
- BDBN inside SMSF
- BDBN strategies inside SMSF

SMSF estate planning – its all about control

What happens when a SMSF member dies and there's no binding death nomination?

Individual trustees

- Person generally ceases to be trustee / member on death
- SIS Act allows executor or administrator of estate to act as trustee on behalf of deceased member
 - not mandatory despite s17A
 - depends on terms of deed and wishes of surviving trustees
- How does control of an SMSF pass in the event of the death of a member/trustee?

Death – individual trustees

Individual trustees

- Death benefit paid in accordance with governing rules
 - Discretion
- Trustees must exercise discretionary powers:
 - honestly and in good faith
 - upon real and genuine consideration and not irresponsibly, capriciously or wantonly
 - with due consideration for the purpose for which it was conferred and not for some ulterior purpose
- Wills irrelevant unless death benefit paid into estate

The *Marsella** case

Recent Victorian Supreme Court case

- The Swanton Superannuation Fund was established in 2003 with Helen Marsella (deceased) and her daughter from her previous marriage, Caroline Wareham as individual trustees.
- Helen was sole member and founder of the Fund until her death
- Helen had a husband (Riccardo) of 32 years.
- Caroline relied upon s41(1) (b) of the Trustee Act 1958 (Vic) to appoint her own husband Martin as co-trustee to satisfy the requirement in the Deed to have a min 2 trustees
- Caroline exercised trustee discretion to pay the entire death benefit to herself.

* Re Marsella; Marsella v Wareham (No 2) [2019] VSC 65

The *Marsella** case

Recent Victorian Supreme Court case

The Court was asked to determine:

- Whether Caroline and Martin properly exercised their discretion when paying the Deceased's death benefit. Whether the trustees acted in good faith, with real and genuine consideration and in accordance with the purposes for which the power was conferred, and
- Whether Caroline and Martin should be removed as trustee and the appointment of a new trustee.

The Court ruled in favour of Riccardo, removed the daughter and her husband as trustee and set aside their exercise of their discretion.

* Re Marsella; Marsella v Wareham (No 2) [2019] VSC 65

The *Marsella** case

Other key learnings

- Is this the death of trustee discretion?
- Trustee must not act in conflict of their duty, but 70% of SMSFs are husband and wives
- Can anyone recall a famous case that's almost identical in facts to this one?

* Re Marsella; Marsella v Wareham (No 2) [2019] VSC 65

Death – individual trustees

Ioppolo & Hesford v Conti

- Husband and wife set up SMSF in 2002
- Deed allowed for trustee discretion and for members to make binding nominations
- Wife later made a Will in 2005
 - named daughters as executors
 - specified super to be paid to her children and not to her husband
- Wife died in 2010
 - no valid binding nomination in place
 - Trust deed provided in the absence of a valid BDBN, death benefits were to be paid at the trustee's absolute discretion.
- Husband reviewed deed and exercised discretion to pay 100% to himself

Death – individual trustees

Ioppolo & Hesford v Conti

- Two of the wife's children were executors of her estate and challenged
 - as executors they should have been appointed as directors
 - husband acted in bad faith by ignoring the will
- Failed on both counts
 - SIS allows for appointment of LPR but does not require it
 - trustee entitled to ignore the will and fact it did so was not evidence of bad faith

Death – corporate trustees

Corporate trustee

- A director automatically loses their office when they die or lose mental capacity
- Enduring Power of Attorney or LPR don't automatically become a director unless the constitution specifically allows it.
- Shareholders can appoint/remove directors
 - Most members generally hold one share each
 - Be mindful of old constitutions, quorum requirements
- Remaining directors often retain control

SMSF estate planning – binding death nomination

“ What you leave at your death, let it be without controversy, else the lawyers will be your heirs.”

Francis Osborne

Legislative framework for BDBN in SMSF

Binding death nomination inside SMSF

- Made under different legislative provisions to BDBN in large funds
- SMSFD 2008/3
 - Governing rules of a SMSF may permit its members to make a BDN
 - Doesn't have to meet SIS Regulation 6.17A (i.e. lapses after 3 yrs., witnessed by 2 person, in proportion etc.)
- What's in the trust deed is paramount

What protection does a BDBN offer?

- Trustees are bound to pay the death benefit to the nominated beneficiary
- Not subject to challenge in AFCA
- A valid BDN cannot be overturned unless:
 - It is invalid
 - It has expired (if there's an expiry date)
 - The person making the nomination was under undue influence or lack making testamentary decision capacity

Other reasons why a nomination may be invalid:

- Nominated person no longer a dependant of the deceased and/or Legal Personal Representative (LPR) just before the member's death.
- Residents of NSW only – notional estate provision
- If the nomination was made by an EPOA and there's deemed to be a conflict of interest
- Only SIS dependants or legal personal representatives can be nominated as a beneficiary

BDBN lessons learnt through past court cases

Donovan v Donovan [2009] QSC 26

- Mr Donovan had a SMSF with a corporate trustee
- The trust deed permitted him as a member to make a binding nomination to the trustee of the SMSF
- Mr Donovan wrote a letter to himself as trustee of the SMSF, advising of his wish that upon his demise the balance of his super to be paid to his LPR
- Mr Donovan later died and it was brought to the court to determine whether his letter to the trustee constituted a binding death nomination

Donovan v Donovan continued...

The terms of the deed:

“...a member may make a binding death nomination in the form required to satisfy the Statutory Requirements; ...”

- The court ruled that the letter did not indicate whether it was binding or non-binding. The letter made no attempt to follow any particular form, and only expressed a “wish” rather than a binding nomination
- The only way to satisfy the “Statutory Requirement” would be to meet the conditions in SIS Reg 6.17A

Key learning:

BDBN must be made strictly in accordance with the requirements of the trust deed of the SMSF

Wooster v Morris case – 2013 Victorian Supreme Court

- Mr Morris (the deceased) had two adult daughters from a previous marriage
- Mr Morris made a binding death nomination in favour of his two daughters in his SMSF
- Mr Morris died in 2010 with approx. \$924,509 in SMSF
- Mrs Wooster (stepmother) and surviving trustee of the SMSF, following the death of her husband did the following:
 - Appointed her own son as a trustee of the SMSF
 - Changed trusteeship of the SMSF to a company
 - Decided that the BDBN was not binding
 - As sole director of Co. trustee paid entire death benefit to herself

Wooster v Morris case – 2013 Victorian Supreme Court

- The daughters commenced legal proceedings seeking to validate the BDBN
- It was ruled that the BDN was indeed valid
- Massive legal & accounting fees – over \$343,000
- Disputed over who would pay this expense, Court ruled
 - All money held by the SMSF (including Mrs Morris's member account) were available to meet this payment, and
 - The trustee and Mrs Morris personally were jointly and severally liable to pay all outstanding money



Key learnings:

When a person dies their executor (LPRs) doesn't automatically become a trustee in the deceased's place

Making an effective binding death nomination

Munro v Munro – March 2015 Queensland Supreme court case

- Mr Munro died at age 66, survived by his second spouse (Suzie) and two daughters from previous marriage.
- After death Mrs Munro appointed her own daughter Ms Pooley as trustee
- Mr Munro signed a BDBN in 2009 to direct the Fund trustee to pay his death benefits 100% to “Trustee of Deceased Estate”
- The Court ruled the BDBN wasn’t a binding death nomination for the purpose of clause 31.2 of Fund deed. Thus, death benefit could be paid by exercise of the trustee’s discretion.



Key learning:

“executor of estate” legally distinct to “trustee of deceased estate”

Wording in the SMSF trust deed paramount

Cantor Management Services Pty Ltd v Booth

- Deceased's brother was the deceased's EPOA and appointed the sole director and shareholder of the corporate trustee CMS.
- Deceased made a BDBN in favour of his "legal personal representative" in 2012.
- Deceased appointed his cousin Dr Booth as the executor of the estate.
- CMS (trustee company) contended that the BDBN was ineffective because it has not been given to the trustee.
- The BDBN was held by the accountant of the SMSF at the registered office of the corporate trustee.
- Court held that it was sufficient to constitute service on the corporate trustee for the BDBN.



Key learning:

Need to ensure BDBN is "served" to the trustee

Making BDBN directly to a beneficiary for asset protection

- **Morris v Morris [2016]FCA 846**

Superannuation fund trustee exercised discretion to pay death benefits to the deceased member's spouse who is bankrupt undischarged. Court ruled lump sum death benefits payments will be protected from creditors provided that the payment were received directly by the bankrupt.

- **Cunningham v Gapes 2017 FCA 787**

Bankrupt person received from deceased's estate a share of deceased's superannuation benefits.

Court ruled that payment is not protected as bankrupt did not have an interest in the superannuation fund.

Key learning:



Superannuation lump sum distributed directly to a beneficiary is protected from bankruptcy trustee.

BDBN strategies

Here's the silver lining

- As s59 and s59(1A) don't apply to SMSFs, then at general law, as long as the governing rules of a SMSF permits, a BDBN within a SMSF could do any or all of the following:
 - Specify how super death benefits are to be paid i.e. lump sum or as an income stream, may even be possible to allow a pension to revert under a BDBN
 - Conditional – e.g. pay death benefits to A if A agrees to certain conditions
 - Cascading – e.g. pay death benefits to A if A survives me by 30 days, otherwise pay entire balance to B
- **Still subject to certain SIS limitations**

Conditional binding death nomination

Case study

- George is a primary producer, and Tom his eldest son have been working on the farming business for a long time.
- George's other children Tina and Mary are not actively involved in the farming business. Unfortunately, Tom doesn't get along with his sisters.
- It is George's intention to leave the farm (\$800k) to Tom, his only other substantial asset is his super of \$1 Million in his SMSF. It is George's intention to leave his super to Tina and Mary.
- George's personal estate consists of the farm, how can he protect Tom from potential family provision challenges from Tina and Mary?

Case study: estate equalisation

Potential solution for George

Having a conditional BDBN in his SMSF to the following effect:

- If Tina and Mary execute a Court approved release of their rights to apply for a family provision order pursuant to the Succession Act 2006 NSW, then his super is to be divided equally between Tina and Mary.
- Otherwise, his super is to be divided 60% to Tom, 20% to Tina and Mary respectively.

Discretionary binding death nomination

- Marco and Ritchie are both members of their SMSF
- They have 3 children (1 financial dependant, 2 independent adult children)
- They each own life insurance policies inside SMSF which are payable in the event of death.

Marco and Ritchie's estate planning goals:

- In the event of their respective death their super benefits goes to each other
- In the event of their simultaneous death, their superannuation benefits will be paid equally to their three children
- they also would like to ensure that as far as is possible each of the children will receive overall an equal split of their super (incl. insurance), net of tax

Discretionary binding death nomination

Potential solution is to give trustee of the SMSF discretion to work out what amount to pay each of their children. The BDBN could be worded to the following effect:

- Pay 100% of my death benefit to my husband/wife if he/she survives me by 30 days
- Provided however if my husband/wife fails to survive me by 30 days then trustee the amount of my super benefit will be paid in the discretion of the trustee... having regard to the extent to which each of my children so as to ensure as far as is practicable that my children will each receive an equal share of the total overall sum of the amounts of my death benefit

Practical consideration for making tailored BDBNs

Essential to review the SMSF trust deed, may require updating in order to:

- Specifically authorise or allow the making of a conditional BDBN;
- Prevent a subsequent amendment to the SMSF trust deed from overriding an existing BDBN
- Prevent the member's Enduring Power of Attorney from amending or revoking the BDBN



“When we are planning for posterity, we ought to remember that virtue is not hereditary.”

Thomas Paine, Common Sense



- Questions???
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- Thank you

Thank you