The Super Death Trap

By **Jocelyn Furlan**

Jocelyn Furlan has been the Acting Chairperson of the Superannuation Complaints Tribunal since September 2007. The views expressed in this article are those of the author and do not necessarily represent the views of the Tribunal.

The Tribunal was established by the Superannuation (Resolution of Complaints) Act 1993 and commenced operation on 1 July 1994. It is an independent dispute resolution body that deals with a range of superannuation-related complaints and offers a free "user friendly" alternative to the court system. The Tribunal can be contacted on 1300 780 808 or via its website at www.sct.gov.au

This article explores three common misconceptions about superannuation death benefits and sheds light on the law as it currently stands. These three common misconceptions may result in unexpected outcomes for the beneficiaries of death benefits payable from superannuation funds, and may end up as complaints to the Superannuation Complaints Tribunal (the Tribunal).

MYTH 1

All nominations of beneficiaries are binding and trustees will always follow them.

This is not true. There are three types of nominations of beneficiaries. The first, and by far the most common, is a "preferred", or non-binding, nomination. Many funds offer this type of nomination. To make it, the fund member must simply complete the information (typically included in a membership application form) and sign it.

The effect of a preferred nomination is to advise the trustee of the superannuation fund of the person/s to whom the member would prefer their benefit to be paid in the event of their death.

However, the decision as to who will receive the death benefit, and how it will be divided if there is more than one potential beneficiary, will be made by the trustee.

The payment of a death benefit from a superannuation fund where there is no binding nomination in place involves two steps.

Firstly, all the potential beneficiaries must be correctly identified – that is – the people eligible to receive all or part of the benefit because they fall both within the definition of "dependant" in the trust deed of the fund that is paying the benefit and within the law[1] – must be ascertained. The trust deed will also usually allow the benefit to be paid to the legal personal representative ('LPR') of the deceased member in their capacity as executor or administrator of the deceased member's estate.[2]

Once the potential beneficiaries have been identified, the second step involves the trustee deciding what proportion of the benefit each potential beneficiary and/or the LPR should receive. In considering who should receive how much, the trustee will consider the wishes of the deceased (for example, the preferred nomination or the terms of the deceased's Will), the financial circumstances and needs of the potential beneficiaries and the nature of the relationship between the beneficiaries and the deceased.

If a member nominates a person or an organisation who does not meet the definition of "dependant" in the trust deed of the fund of which the deceased is a member, no part of the benefit will be able to be paid to the nominated beneficiary. For example, if a member nominated a charity as their preferred beneficiary, the trustee would not be able to pay the benefit directly to that charity. However, the member may be able to achieve this outcome by nominating her or her estate (or legal personal representative in their capacity as executor/ix of the estate) and then providing for the charity in his or her Will. However, caution needs to be exercised here. If there are dependants who survive the member, the trustee will consider their needs and the financial arrangements between them and the deceased, and may determine to pay the benefit directly to the dependants rather than to the estate, even in the face of a different preference of the deceased.

Given that a preferred nomination is not binding the question that sometimes arises is – what is the point of making a preferred nomination if it is not binding? The value of the nomination is twofold – firstly, it may alert the trustee to the existence of a potential beneficiary of whom it might not otherwise be aware, and secondly, it provides an indication of the member's wishes, which is one factor that the trustee will take into account in determining how the benefit will be paid. (As noted above, others include the terms of the member's Will and the personal and financial relationships between the parties).

The second type of nomination is a binding nomination. A binding nomination, if it is valid, is binding on a trustee and a trustee must distribute a death benefit in accordance with the nomination. The requirements of a binding nomination involve a number of procedural steps as set out in Reg 6.17A of the *Superannuation Industry (Supervision) Regulations* 1994.

The nomination must be in writing; and must be signed and dated by the member in the presence of two witnesses, each of who is 18 or older and neither of whom is mentioned in the nomination as a beneficiary. It must also contain a declaration signed, and dated, by the witnesses stating that the member signed the notice in their presence.

A nomination is only valid for three years, and therefore will lapse if it is not renewed every three years.

Many people are of the view that they have completed a binding nomination. However, once a person becomes aware of the requirements for a valid binding nomination, he or she will usually realise that the nomination completed is not a binding nomination, but is in fact a preferred nomination.

Further, not all superannuation funds offer binding death benefit nominations.

Like a preferred nomination, to be valid, a binding nomination can only be made in favour of a dependant or the legal personal representative of the member. If a binding nomination purports to direct a trustee to pay all or part of a death benefit to a person who does not meet the definition of dependant or is not the legal personal representative, the nomination is invalid and the trustee will not act on it.

If a member wishes their superannuation to go to a person or organisation that does not meet the definition of "dependant" in the applicable trust deed, one way would be to make a binding nomination that the benefit be paid to the legal personal representative for the benefit of the estate, and then bequeath the superannuation amount in the Will.

The third type of nomination is a non-lapsing binding nomination. Section 59(1)(a) of SIS allows a person to direct a trustee as to whom a death benefit is to be paid, but only if the trust deed of the fund provides that the trustee consents to directions in death beneficiary nominations. Some funds include this provision to allow this type of binding nomination. It is subject to the same restrictions as the other types of nominations i.e. it can only be made in favour of those persons who are eligible to receive the benefit under the trust deed or the law.

Given the different types of nominations and their different consequences, it is important that fund members read the fund documentation and understand the type of nomination they are making.

MYTH 2

Superannuation forms part of a member's estate and can be dealt with in accordance with the member's Will.

This myth is also not true. Superannuation does not form part of a person's estate. Broadly, the purpose of superannuation is to provide income in retirement to members and their dependants. In the event of death before retirement, the author's view is that the superannuation death benefit should be paid to dependants and those who had a legal or moral right to look to the deceased member for financial support had he/she not died. The ability of a superannuation fund to pay a tax-free death benefit directly to a dependant rather than to the estate has a number of advantages. Firstly, it ensures that the benefit is paid directly for the benefit of the dependant(s) and is not available to creditors of the estate who would be paid first from the assets of the estate. Secondly, it can usually reach the beneficiaries quicker than if a grant of probate or letters of administration has to be obtained and the estate called in and distributed. Thirdly, as a general rule, superannuation death benefits are protected from bankruptcy. Accordingly, even if the deceased member was bankrupt, or if his/her estate is insolvent, funds can be paid direct to his/her dependants to replace the income stream that may lost as a consequence of the death.

Some commentators argue that the concept of dependency in relation to superannuation death benefits is less appropriate in a society with increasing rates of multiple relationships and financial literacy, and that superannuation should always be paid in accordance with a member's wishes as set out in his/her Will. However, there is little evidence to show that the Australian population is well educated in the area of regularly executing and updating their Wills to reflect their changing circumstances[3]. Further, it is not difficult to conceive of the average Australian

superannuation fund member whose only significant assets are a jointly owned family home (which automatically passes to the survivor) and superannuation. The advantage, shortly after an unexpected and untimely death, of tax free funds being directly available for dependants to assist them in continuing to meet day to day living expenses previously covered by the member's wages, without the necessity of incurring expense and delay in sorting though estate issues and implementing procedures to enable distribution of the estate, is in the author's opinion a significant and valuable feature of the current system, and would apply to the vast majority of Australians.

MYTH 3

Superannuation is for the payment of funeral expenses

The Tribunal receives complaints from a deceased member's loved ones complaining that they feel entitled to receive all or a portion of the deceased member's death benefit because they paid for the funeral. Typically, a parent has paid for a child's funeral and claims reimbursement of the cost of the funeral from the superannuation (particularly if the estate has no assets).

The difficulty is that, if the parent does not come within the definition of "dependant", (either because they are not in a dependent or interdependency relationship with the deceased or because they are not fully or partially financially dependent on the deceased), they will not be included as a possible beneficiary of the deceased member's superannuation. The fact that a person pays for a deceased member's funeral will not of itself bring that person within the definition of dependant. In these circumstances, the only method by which the funeral expenses could be recouped is if all or part of the death benefit is paid to the estate and the estate could then reimburse the cost of the funeral.

In the author's view, however, this is only desirable where there are no potential dependants because payment of the death benefit to the estate could also result in payment to other creditors prior to the balance being distributed to the beneficiaries.

If a person chooses to pay the funeral expenses of a deceased member, they should do so in the knowledge that there is no automatic right of recovery of those funeral expenses from the superannuation death benefit. Likewise, if a person wishes to ensure that the costs of their funeral will be covered, appropriate planning may be of benefit. An assumption that the superannuation will cover the cost may not be borne out.

CONCLUSION

The area of superannuation is complex and constantly changing. This article has attempted to highlight some of the more common myths about superannuation that continue to persist, and offer some comments about how superannuation death benefits currently operate.

CASE STUDY

One case that came before the Tribunal is a good example of the conflict that can arise between a member's wishes and the needs of dependants. In case D07-08\102, the sister of the deceased (who was also the joint executrix of his estate) complained to the Tribunal about the trustee's decision to pay the whole of the death benefit to the wife of the deceased, on the grounds that the decision conflicted with the deceased's stated wishes. She sought for the benefit to be paid to the legal personal representative for distribution in accordance with the deceased's Will.

The deceased was diagnosed with a brain tumor in July 2006. He arranged for an application to be made to the fund for the early release of his superannuation balance on the grounds of permanent invalidity and ostensibly opened a bank account for the superannuation to be paid into.

He did not make a binding nomination, although he could have.

In August 2006, he executed a new Will, just 11 days before he died, aged 48. The Will purported in broad terms to divide his superannuation benefits between his wife, his mother and two sisters, and left his other property to his wife.

He died before the superannuation benefit was paid and it became a death benefit of a larger amount because the death benefit insurance component also became payable.

The sister argued that the trust deed of the fund permitted payment to the legal personal representative as well at to dependants and did not provide a system of priority where one beneficiary should be preferred over another. She placed great emphasis on the wishes of the deceased as expressed in his final Will and argued that the wife was financially secure because of the other property she inherited.

The deceased had been married to his wife for 16 years at the time of his death and they were living together at the time of his death. There was no evidence of any marital problems. The wife was financially dependent on the deceased – all income, costs and assets were jointly owned or shared. Conversely, neither the sister nor any of the other relatives named in the Will had any financial relationship at all with the deceased – they were not financially dependent on him. They thus had no legal or moral right to look to him for financial support had he not died.

The Tribunal in arriving at its determination noted that it was "faced with a comparison of the Deceased Member's wishes with the circumstances – he was not financially supporting anyone other than the Wife. Had he not died, it appears that he would have continued to financially support his wife to the exclusion of all others" and they would have used his superannuation to fund their retirement together.

The Tribunal affirmed the trustee's decision as fair and reasonable in its operation in relation to the Complainant in the circumstances, even though the Tribunal accepted the evidence of the deceased's wishes that the benefit be split between his wife, the sister, his mother and another sister.

Had the deceased made a binding nomination in favour of his estate, his wishes would have been realised. In spite of this, the Tribunal was unable to find that a decision to pay a dependant was unfair or unreasonable in relation to other people who would have received a "windfall" because their financial situations were not adversely affected by the deceased's death.

NOTES

1 "Dependant" is defined in section 10 of the *Superannuation Industry (Supervision) Act* 1993 ('SIS') as including the spouse of the person, any child of the person and any person with whom the person has an interdependency relationship. It includes a person who was in fact dependent on the member. All trust deeds usually also contain a definition of "dependant".

2 For example, a typical trust deed will usually contain a payment clause similar to the following:

"The Trustee shall hold a Member's Death Benefit UPON TRUST to pay the same to such one or more of the following persons to the exclusion of the other or others and in such manner and proportions as the Trustee determines, namely:

(i) to the Member's dependants; and

(ii) to the legal personal representative of the Member; and

(iii) to any other person to whom payment of the benefit is permitted under the Relevant Law; …"

3 The NSW Law Reform Commission Report 116 (2007) – Uniform Succession Laws: Intestacy suggests that intestacy occurs quite frequently in Australia, and approximately 20,000 of 46,000 deaths in NSW do not come within the Probate Division.

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