



## YOUR GUARDIAN

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### “To Bind or Not to Bind.....”

Hamlet spent arduous hours pondering existence and death. One wonders if he put as much thought into the distribution of his wealth after death.

Throughout the ages, the legal system has recognised individuals rights to control the distribution of their wealth after death through some form of Will or Binding Nomination.

Today in Australia, the Legal System separates the individuals' personal assets from their superannuation. Broadly speaking, upon death, personal assets are pooled into the Estate and the Executor named in your Will distributes them based on the Will or the Public Trustee takes charge if the person dies intestate. **However, superannuation savings can be directed straight to a beneficiary and bypass the estate.**

This newsletter focuses specifically on distribution of superannuation monies upon death and does not address individual estate planning and Wills. We will focus on Binding Nominations and the recent changes to allow a Binding Nomination to be valid in perpetuity rather than having a 3 year limitation.

### Distributing Superannuation Savings on Death

As superannuation savings can make up a very large chunk of your personal wealth, its imperative that due consideration is given to what happens to this money when you die.

Upon your death, any money held in superannuation needs to be distributed by the Trustees. In a self managed fund, your Legal Personal Representative (LPR), which is generally the Executor over your Estate, will step in as temporary Trustee over the SMSF and act with any surviving Trustees to liquidate the fund assets and make the death benefit payment.

The default position (if there is no Binding Nomination or Reversionary Pension), is that surviving Trustee(s) can distribute the money to any persons that satisfy the definition of a Dependant under the Legislation, or to the Estate.

Allowing surviving Trustees to determine how the distribution is made can have some risk, especially if there are competing claims by family members (or de-facto's / adult children / children from previous marriages) for part of your super balance or a contestation of the personal Will.

Before you die you are able to nominate who you would like to receive your superannuation money, and elect to make the nomination 'Binding' upon the surviving Trustees to ensure the money goes where you wish it to go.

### Nomination of Beneficiary

A 'Nomination of Beneficiary' is a direction that a member provides to the Trustee of the super fund in relation to distribution of his or her funds on death. It can be done by a simple one page document setting out the member's preference and appropriately signed and witnessed. A member can choose to make:

1. **A Binding Nomination:** The Trustees MUST pay the death benefit as nominated.
2. **A Non-binding Nomination:** The Trustees have the discretion to follow the stated wishes of the member or direct the entitlements to another person (or persons) or pay the entitlement directly to the Estate.
3. **No Nomination:** If you do not make any nomination, you are not breaking any Laws. The surviving Trustees simply have full discretion to distribute the funds to the Estate or any Dependant that they chose.

### Who can I nominate?

There are restrictions on who you can nominate under the Superannuation Industry Supervision Act (SIS). Valid nominations can be made to:

1. the Legal Personal Representative in which case the benefit is paid to the Estate; or
2. a Dependant which is defined as follows:
  - Spouse (current or de facto or former spouse and can include same-sex and living with a person in a genuine domestic basis in a relationship as a couple);
  - A child of the member (including adopted, stepchild, ex-nuptial, child of your spouse);
  - Any other person with whom the member has an interdependency relationship, which covers persons where there is a close personal relationship and one or more provides the other with financial support, domestic support and personal care. We recommend seeking advice if you have circumstances that you think may qualify.

Common mistakes that we see are Nominations being made to parents, brothers or sisters or other relatives, but there is no interdependent relationship so the Nomination is invalid.

A Nomination can have “if, then” clauses to allow you to nominate persons should certain beneficiaries have already passed away – such as

“100% distribution to my spouse. If I survive my spouse, or if I divorce from current spouse, then distribute to my children on equal proportionate basis”.

## Can I Nominate Grandchildren?

A grandchild might be able to be nominated if they have an interdependent relationship with the member.

Some of the more aggressive strategies suggest that by paying school fees for grandchildren that there is financial dependency. The test also requires that they are living together and that one of the persons provides personal care to the other. Whilst these circumstances are possible, they are not generally common. Nevertheless, lifestyle changes can be made such that you do meet the requirements of the definition. Also note that the definition does not define how long that arrangement needs to be in place so it may be possible to create such circumstances when nearing death although this is untested and not recommended as a strategy to adopt.

The Legislation here is subjective and members should take a cautious approach and seek legal assistance. We also find that there is some caution in allowing benefits to flow through to young grandchildren who may not be of a mature age to invest funds appropriately.

## Why Bind?

The obvious reason to ‘Bind’ is to ensure the money goes where you specifically want it to go and take away any discretion that the surviving Trustee would otherwise have.

### Example 1- No Binding Nomination

*Greg has an SMSF with \$1M in assets when he died. He was the sole member and director of the corporate Trustee. He was remarried and has 2 children with his former spouse and 1 expectant child with his current spouse. His estate is administered by his first child, Adam.*

*The default position here is that Adam acts as LPR and steps in as Trustee. If he didn’t find a Binding Nomination, he can distribute the funds to any dependant that he chooses:*

*He could do the following:*

- *Distribute all of the money to himself – he qualifies as a Dependant under the SIS definition.*
- *Distribute the money to himself, his mother (former spouse) and his sister and exclude Greg’s current wife and expectant child.*
- *Distribute to the estate and then handle it through the estate which he is administering as part of the Will.*

### Example 2 – Outdated Binding Nomination

*Adam then found a Binding Nomination that Greg did 2 years ago, before he split from his first wife. At that stage he simply nominated his spouse. He did not write her name on the form, it simply said “100% spouse”. At the time he wrote it he was obviously referring to his former spouse and that’s the view that Adam is taking as he considers making the distribution. However a literal interpretation would suggest the form relates to his current spouse. In this case we would expect the new spouse to contest the distribution and legal support would be necessary.*

### Example 3 – Current Binding Nomination

*When Greg remarried, he wrote up a new Binding Nomination held by the fund administrators. The new nomination stated “50% to all of his surviving Children in equal proportions and 50% to his current spouse”. Greg has managed to look after those he holds dearest and exclude his former spouse. Legal assistance would be necessary in relation to the Splitting of the 50% Children portion due to the unborn child.*

## Is it always a good idea to make it binding?

There are circumstances where making a Binding Nomination might not be such a good idea, such as:

- You do not have any Dependants or any family concerns;
- If the beneficiaries include adult children (aged over 18 or if full time student aged over 25), the taxable portion of the member balance will be taxable to the recipient at 15% plus Medicare levy. The death benefit might be better managed by allowing the LPR to have discretion in the distribution to minimise the tax impact;
- Circumstances changed after doing the Binding Nomination such as marriage breakdown and you didn’t get around to changing it; or
- One of the beneficiaries falls into financial difficulty or addiction and you do not wish for them to use the money to cover their personal debts or habit.

## How long can a binding nomination last?

The SIS Regulations include a 3 year restriction on the lifespan of a Binding Nomination. However, last year the ATO released a Determination that this Rule does not apply to self managed funds. Therefore, whilst a Binding Nomination for a member in other forms of super can only have a 3 year lifespan, in an SMSF the binding nomination can remain in force in perpetuity.

Most Binding Nominations for SMSF’s make no mention of the lifespan that the Nomination is to last. Prior to the ATO Determination, the industry view was that it expired after 3 years like other forms of super.

However, since the ATO Determination, the nomination lasts until it is revoked provided the Trust Deed does not restrict its lifespan.

The benefit of having a non-expiring Nomination is that you don't have to worry about updating it every 3 years. However the risk is that the member does not make a change to the Nomination should there be a change in circumstance.

## Can a Binding Nomination be changed should I become incapacitated?

The rights of a Power of Attorney (POA) acting for an incapacitated member are not clearly defined in legislation and may vary from state to state. Generally a POA has no legal right to form a Will for an individual, and may therefore be unable to create or revoke a Binding Nomination.

On this basis, it is a good idea to update your Binding Nomination as soon as any changes are needed. If the POA has no rights then it may be your advantage that they cannot form a Binding Nomination or revoke an existing one. On the other hand, if the existing Binding Nomination is no longer valid, for example due to the death of the beneficiary, the POA may not be able to create a new Binding Nomination.

As this is unclear we recommend legal advice.

## The impact of a Reversionary Pension

When establishing a pension, the Trust Deed may allow you to determine that upon your death, the pension is to continue, and be paid to a nominated dependant – called a Reversionary. It is common to see a Reversionary pension set up so that payment is made to the spouse on the death of the member which allows the money to be retained within the Superannuation fund until that member dies.

## What happens if the Reversionary differs to the Nominated Beneficiary?

There is no specific legislation that determines which takes precedence on death of the member. It is the Trust Deed that creates these powers, so if the Deed specifically identifies which takes precedence the Trustees must follow it. However most Deeds are silent on this matter, in which case the legal opinion is that since the Reversionary Pension is a contract, it continues after death and there is no death benefit to be paid. In other words, the Reversionary takes precedence over the Binding Nomination unless the Deed states otherwise. If you have a Reversionary pension it is important to update it if your preferred beneficiary changes.

### Example 4 – Binding Nomination differs to reversionary pension

*Greg's pension was initially set up with his previous wife as reversionary, and he has since remarried but his pension is still running. On his death, the first wife may claim that the pension reverts to her. The Binding Nomination may however state that the death benefit payment is to the new wife. The words contained in the Trust Deed would need to be followed to determine which takes precedence, and if silent then his first wife may lay legitimate claim.*

We therefore recommend that whenever there is a significant family change, you should review both the Binding Nomination and the Reversionary Pension, if there is one, to ensure there is consistency. Estate planning and legal advice may also be necessary.

## The Trust Deed

The Trust Deed should be drafted to cater for flexible nominations. It may be that many Deeds are too prescriptive with their clauses and this could limit the type of nomination allowed.

The starting point for trustees is to review the rules set out in the Deed.

For example, the Deed may:

- specify that all death benefit payments are to be paid as a lump sum to the estate; or
- limit the payment of death benefits to certain potential beneficiaries; or
- only allow binding nomination to last for 3 years.

Some lawyers believe a one page nomination form is insufficient and recommend a more detailed nomination made through the Deed, especially in tricky family situations. Note however, that if you elect to do so the Deed would need amendment as the nomination changes which is a more complicated and costly process than simply replacing a Binding Nomination form.

The operation of the Nomination will depend on the Terms of the Deed. Before enacting any Nomination, or activity in the fund, the Terms of the Deed need to be considered.

## Conclusion

Making a Binding Nomination depends on your specific circumstances at the time. You are able to revoke it and change it at any time. It should also be considered as part of your estate planning strategy and we recommend seeking legal advice prior to making your Nomination.

For more information relating to any topics covered in this edition of Your Guardian, call **Brendan Daw** of our office on **1300 787 576**.



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