

SMSF stuff ups beyond the grave

ASF Audits Technical Seminar



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1. Member v death benefit
2. BDBNs as reversionary pensions
3. Incomplete/missing trust documents

Member benefit v death benefit

Overview

1. Why do we care?
2. Who will benefit from death bed member withdrawal?
3. Practical issues when planning and implementing
4. What steps should we take now?
5. Checklist

Why do we care?



Member benefit

- Payment to you
- Because you are member

Death benefit

- Payment to you
- After another person's death
- Because other person member

Member benefit or death benefit?

- Don member and director of trustee of Top Trumps SMSF
- Large cash balance in Fund
- Don given days to live
- Transfers cash from the SMSF to Don's personal account while Don is still alive

Member benefit

Member benefit or death benefit?

- Same facts but this time....
- No benefit payment or benefit payment occurs after death

Death benefit

Why do we care?

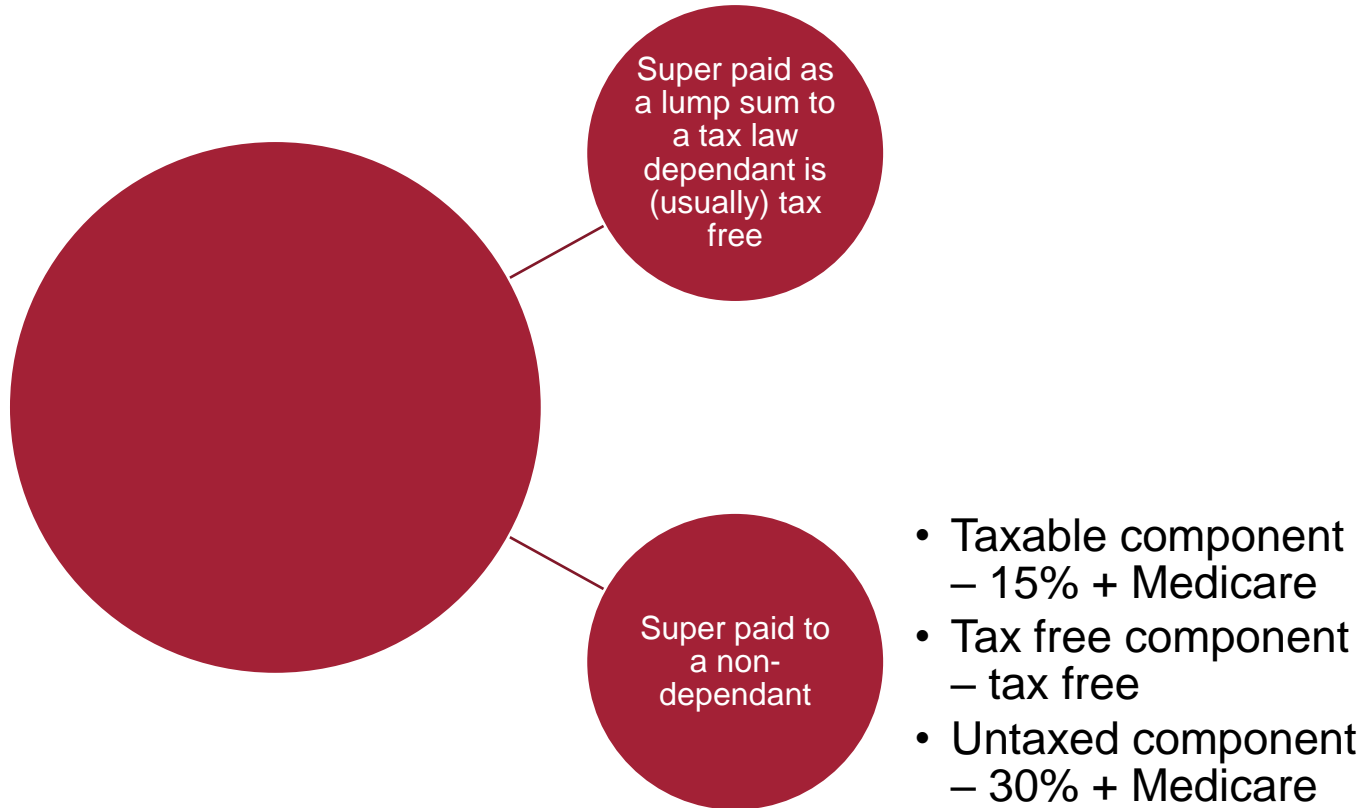
If member aged 60 and 'retired'
then:

- can access super tax free

If member aged 60 and retired
dies with member balance then

- tax could be payable on death benefits

Tax on death benefits



Why do we care?

We don't if:

- Beneficiary is tax dependant
- High tax free component (low taxable)

We do if:

- Beneficiaries not tax dependants
- High taxable component

Super is low
tax
environment

ATO current position

- Once the trustee knows the member has died, becomes a death benefit
- Difficult in SMSFs to have a member benefit if paid after member's death

PBRs – ATO old position!

Death benefit

- 1011912974150 (2011)
- 1051918745226 (2021)

Member benefit

- 1051437446368 (2018)
- 1051598540809 (2019)
- 1051754180223 (2020)
- 1051914995135 (2021)

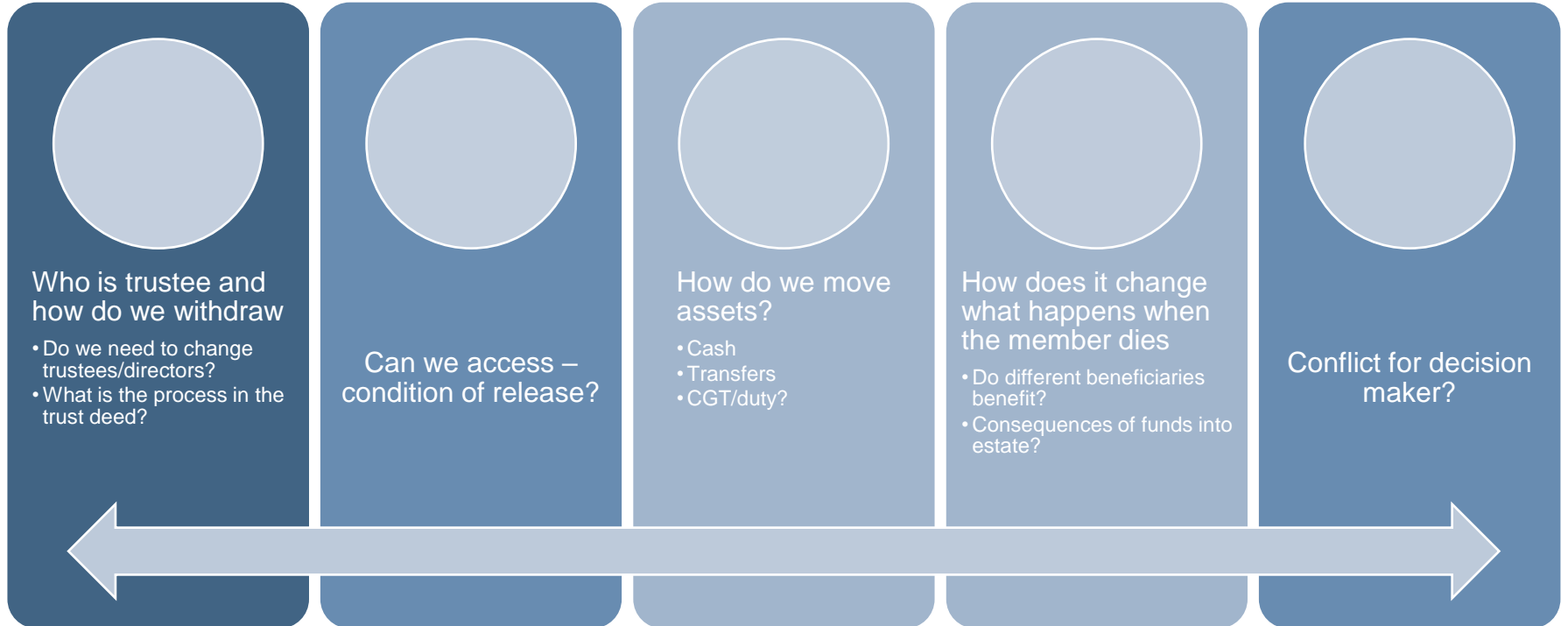
SMSFA discussion with ATO:

ATO settled position is that a benefit payment should be treated as a member benefit where the member has requested the benefit payment prior to their death, despite the benefit being paid after their death

What needs to happen?

- Member benefit
 - Assets/cash transferred to member before death
- It depends
 - Withdrawal triggered before death and completed shortly after death – scope to argue in some cases?
- Death benefit
 - Journal entry used to ‘transfer’ benefits
 - Undated withdrawal request found after death
 - Did not follow trust deed process so ineffective
 - Trustees had lost capacity so no one to make benefit payment decision

Considerations



Example

- Don's BDBN is to his wife Melania
- Don's estate leaves his assets between his 5 children
- If Don withdraws his superannuation immediately before his death...
 - BDBN to Melania is ineffective/useless as no longer any super
 - Super instead forms part of estate and goes to the children

Example

- Don has a stroke and is in a coma
- His daughter Ivanka withdraws all his super from his SMSF using an enduring power of attorney
- Don recovers...
- Who benefits?

Example

- Don requests a full commutation of his pensions
- Then sell assets – CGT liability
- No longer in pension phase – no more ECPI
- Must either
 - Trigger CGT events before request commutation
 - Request part commutation only of pensions

Checklist

1

Who is requesting?
Who is the decision maker?
Will they do what we want?

4

Accumulation / pension
accounts – timing!

2

What do our documents say,
allow us to do or not do?

5

Are there other tax / duty
considerations?

3

What are the assets we are
dealing with / transferring?

6

What can we do now?
What is the effect on estate
planning?

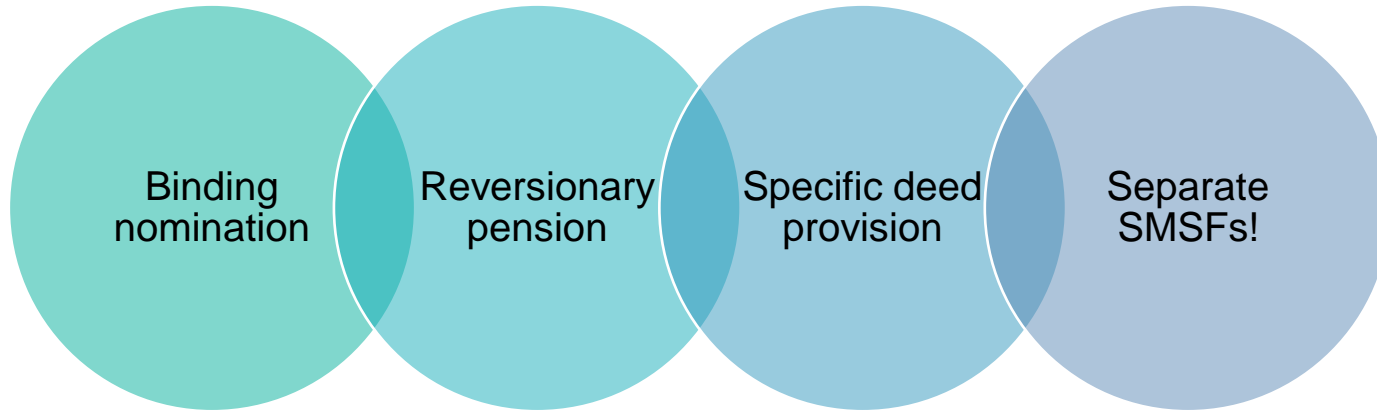
BDBNs as reversionary pensions

Super and estate planning – the starting point!

- Super death benefit does not automatically go under a Will
- Trustee discretion (SIS Reg 6.22)
 - “dependants”
 - spouse
 - children
 - financial dependants
 - interdependency relationship
 - estate
- BDBNs are a common way of removing the discretion



How do we 'lock-in' a benefit



Allows member to lock in decision



Useful in the right situation



Dangerous in others

BDBNs

- Trust deed contains, not SIS
- Regulation 6.17A and section 59 do not apply to SMSFs
- *Hill v Zuda* (recent High Court decision)
- Always follow trust deed
- Is there any room for argument?
- Amend so is certain
- Read it like you are trying to undo it
- Don't just assume the trust deed will allow

Death benefit pensions – 2 types

Auto-reversionary (automatically continue)

- No trustee discretion

Choose to pay as a pension

- Spouse
- Child
 - Under 18
 - Under 25 and dependant
 - Disabled
- Financially dependant
- Interdependency relationship

Can a BDBN = a reversionary pension?

- ATO

- No!
- BDBNs only say to whom
- Leaves trustee discretion as to how

- BUT

- BDBNs can say to whom AND how
- Carefully worded
 - ‘as a continuation of my existing pension’
- Trust deed terms?

Reversions – can we change?

- Stop and restart
- Without?
 - ATO No I mean Yes
 - Arguably if pension terms and trust deed allow



BDBNs v reversionary pensions

- BDBN

- More flexible
- Easily revoked and changed without adverse consequences
- BDBN can be prepared in contemplation of a member receiving a pension
- Can be modified to include contingency events and tailored provisions
- Transfer balance cap

- Reversionary pensions

- Change while pension is current? Could cause a components issue if pensions are stopped and re-started
- Can only be prepared if the member is actually receiving a pension
- Limited ability to tailor
- Ensure can produce pension documents to prove reversion
- Transfer balance cap

Example

- Don is about to draw a pension
- Relationship with Melania is um rocky
- Wants to be able to revert/unrevert as necessary
- Use a BDBN
 - To Melania
 - As a continuation of his pension
 - Can change if necessary

Example

- Don is about to start a pension
- Adviser does not ask Don whether it is to be reversionary or not
 - Makes it reversionary to Melania
- Don goes to see estate planning lawyer
 - Wants all assets to go to their son Barron
 - Nothing to Melania
- But what about the reversionary pension?
- Easier to unrevert if a BDBN

Summary

Trustee discretion
for death benefits
can be
challenging

BDBNs and
reversionary
pensions are both
good answers

Sometimes!

Consider a BDBN
as an alternative
to a reversionary
pension



Missing/incomplete fund documents

Trust deeds

- Set out the rules, including
 - Trustee changes and variations
 - Trustee powers
 - Borrowing
 - Reserving
 - Member rights
 - Benefit payments
 - Death
 - Pensions

Application by Ellasil Pty Ltd [2023] VSC 69

- Originally 2 member SMSF – both deceased
- 3 surviving adult children
 - Separate FPA proceedings settled
- Net assets of \$775k
- SMSF controlled by lawyer for deceased members
- Trustee applied for directions to confirm:
 - It was validly appointed as trustee
 - Whether later variation deed effective
 - Validity of BDBNs from members

Application by Ellasil Pty Ltd [2023]

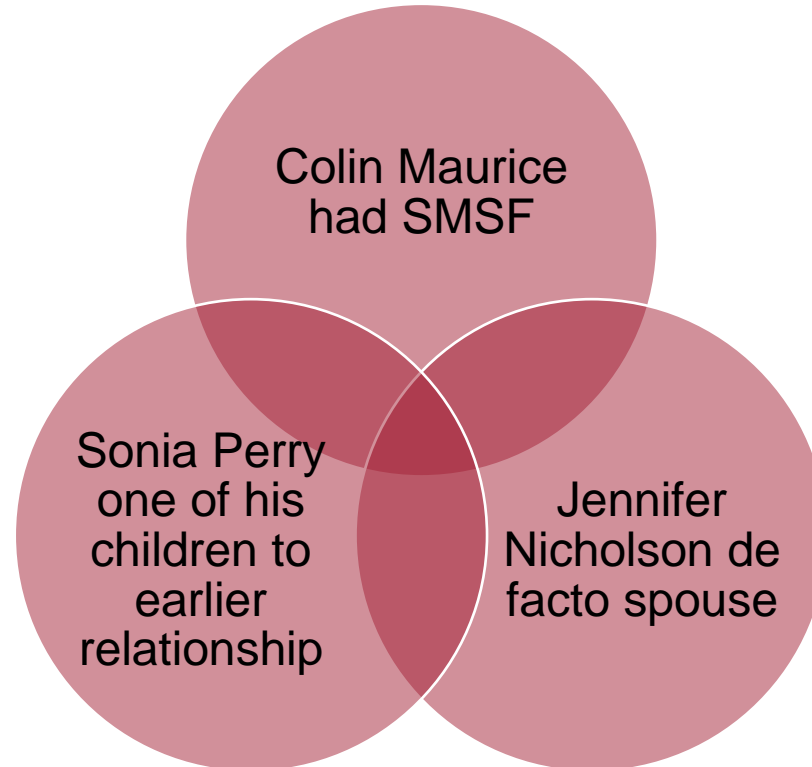
VSC 69

- SMSF likely established in 1979
 - Original deed could not be found
- Some amending documents available
 - Many gaps in chain
 - Earliest from 1989
 - Most recent likely from 2015
- Other documents relating to administration of SMSF
 - Minutes of meetings, financial statements
 - 4 sets of BDBNs prepared by members over years (undated, 2006 x2 and 2017)

Court determined:

- Original deed signed around 1979 and (even though cannot be located) included:
 - Variation power
 - Power for principal employer to change trustee
- Weight of evidence suggests Ellasil validly appointed as trustee and justified in continuing to act as trustee
- Most recent BDBN (from 2017) applies even though suggests only the member's "wish"
 - All remaining entitlements to one child
 - Court "comforted" as reflects terms of Will

Perry v Nicholson [2017] QSC 163



Perry v Nicholson

April 2015 change
of trustee minutes
removing daughter
and appointing
spouse prepared
by accountants

January 2017
BDBN to spouse

Colin dies March
2017

Late 2016 Colin
diagnosed with
melanoma

February 2017
accountants
prepared change
of trustee deed,
dated April 2015



Perry v Nicholson

- Daughter challenged change of trustee in April 2015
 - She was still trustee (and made death benefit decision)
 - BDBN invalid
- Court upheld change of trustee (just)
- If not, death benefit planning would not have worked

Re Narumon

- Original deed + several variations
- Unclear which variations were effective (if any)
- Varied trust deed using powers in all deeds
- Original deed and final variation upheld

So...

Make sure the chain
of trust deeds and
trusteeship cannot
be broken

Or else

- Who is the trustee?
- Who can make decisions?
- Death benefit documents done effectively?
- Have decisions been made?

If there is a problem...

- Fix it now
- Confirm what has happened before
- If cannot fix?
- If going to be an argument?
- Roll to a different fund

Conclusion

Paying benefits
before death –
ATO current view

Paying benefits
before death –
pros and cons

Options for
locking in death
benefits

BDBNs can
mimic a
reversionary
pension

BDBNs can be
more flexible than
a reversionary
pension

Is the trust deed
chain intact?

Any questions?





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