

## the Right money in the Right hands at the Right time



## Making the right super beneficiary nomination

30 January 2017

**Binding and reversionary nominations can help you achieve greater estate planning and social security certainty.**

### Important Note:

*We refer to the recently introduced pension transfer cap of \$1.6m in this article. However, we do not address any other measures covered in the super reforms.*

### Background

For many, your super not only represents a substantial part of your total wealth, it can help ensure your family and certain other beneficiaries are looked after in the event of your death.

But unlike many other assets, super generally doesn't form part of your estate (unless the member's Legal Personal Representative is nominated) and certain restrictions apply to who can receive a deceased member's death benefit.

In simple terms, a super death benefit can only be paid to a 'SIS dependant'.

These include a:

- spouse<sup>1</sup>
- financial dependant
- legal personal representative of the deceased fund member.
- child<sup>2</sup> of any age
- interdependent person

In the absence of certain death benefit nominations, the trustee generally has the discretion to decide which of these dependants will receive the death benefit. As a result, the death benefit could be distributed in a manner that doesn't reflect your wishes.

### How to remove trustee discretion

One way to remove trustee discretion is for you to complete a **binding death benefit nomination**.

This is a legal instrument that enables you to specify which SIS dependant(s) you want to receive your super death benefit and (usually) in what proportions.

Provided the nomination is valid, these dependants can receive the death benefit as a lump sum. However, some SIS dependants will also have the option to receive the death benefit as a pension, where a new pension will be started.

These people include a:

- spouse<sup>1</sup>
- child<sup>2</sup> under 18 years of age<sup>3</sup>
- child aged 18 to 25 who is financially dependent<sup>3</sup>
- disabled<sup>4</sup> child
- financial dependant (other than a child), and
- interdependent person.

*1; Includes a de-facto spouse and same sex partner.*

*2; Includes a natural, step or adopted child, as well as a child of a same sex couple.*

*3: A pension paid to a child will need to cease at age 25, unless they are disabled at that time (see definition of 'disabled' in footnote 4).*

*4: Disabled for this purpose means a person with a disability that's attributable to an intellectual, psychiatric, sensory or physical impairment or a combination of such impairments. The disability must be permanent (or likely to be permanent) and result in a substantially reduced capacity for communication, learning or mobility, and the need for ongoing support services.*

Another option available to those with account based pensions is to complete a **reversionary beneficiary nomination**.

This option enables you to select who you would like to continue receiving your pension payments in the event of your death. These include the same people who are eligible to receive a death benefit as a new pension (as per above).

When assessing these two options, it is important to consider your specific circumstances, including your need for flexibility and other factors.

### When a binding nomination may be more suitable

1. A binding nomination can be more suitable if you want to give your SIS dependant(s) the flexibility to decide whether they want to receive the death benefit as a lump sum or (where eligible) a pension.
2. A binding nomination will be more appropriate if you want the death benefit to be paid to your legal personal representative or if you wish to nominate more than one SIS dependant. With a reversionary beneficiary nomination, the pension can only be continued by a single eligible beneficiary.
3. If your circumstances or preferences change prior to your death, you can amend your binding nomination at any time, provided you have not lost capacity.

Conversely, if you want to change a reversionary nomination, sometimes you may need to cancel and restart the pension, which could have adverse social security consequences if the account based pension is grandfathered.

**Note:** *Certain funds may offer an option to add and remove reversionary nominations without having to cease and restart an existing pension.*

### What types of binding nominations are available?

If a binding nomination is more suitable for you, there are generally two options available – a lapsing and a non-lapsing nomination.

**Lapsing nominations** are valid for three years and must be renewed or they will become invalid.

These nominations may be updated or cancelled at any time to take into account your changing circumstances.

To be valid, the nomination needs to be in writing. It also needs to be signed and dated by you in the presence of two witnesses (who are 18 years of age or older and aren't beneficiaries).

Funds generally allow you to nominate more than one beneficiary and specify a percentage payable to each beneficiary. If more than one beneficiary is nominated, the total nominations must add up to 100%.

**Non-lapsing nominations** are similar to lapsing nominations except they don't need to be renewed after three years to remain valid.

When using either of these options, it's important you keep your nomination up to date, especially if your wishes or personal situation changes and/or a nominated beneficiary ceases to be a dependant for SIS purposes.

Funds which offer non-lapsing binding nominations could offer greater succession planning certainty to 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 you. 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 at the time of death.

### What's a non-binding nomination?

These are death benefit nominations that are offered by some super funds (in particular SMSFs) where you can nominate who they'd like to receive your super in the event of your death.

This arrangement can be beneficial when it is desirable to have flexibility at the time of death (eg to pay the death benefit to the estate or to a beneficiary or to pay multiple death benefit pensions to multiple dependents).

This type of nomination provides guidance for the trustee when deciding which SIS dependants will receive the death benefit. However, unlike lapsing and non-lapsing binding nominations, the trustee still has the discretion when making this decision.

### When a reversionary nomination may be more suitable

1. A reversionary nomination may be more suitable if the deceased member and/or your beneficiary require greater certainty that a pension will continue to be paid after death. The beneficiary will receive the next regular payment with no interruption.
2. It is possible for the binding nominations to become invalid at the time of death. This could occur, for example, if the member forgets to update the nomination when your circumstances change or they fail to renew a lapsing nomination. This is unlikely to occur with reversionary nominations.
3. With a reversionary nomination, the beneficiary doesn't have to decide how they want to receive the money at a time of grief and the funds are retained in the concessional taxed super environment.

This can help ensure a beneficiary who intends to receive the death benefit as a pension does not mistakenly take the money as a lump sum. This can be mainly important for dependants who aren't eligible to make super contributions.

Also, you may be adversely impacted by the social security income test if the funds leave the super environment (see case study 1 on page 3). It is important to note that the pension can be commuted at a later point if a lump sum is required.

4. A non-reversionary pension that commences for an eligible dependant on your death is treated as a new super pension by social security and is deemed for income test purposes.

This may have a negative impact on pensioners who are affected by the income test.

If the account based pension is grandfathered for social security purposes (eg not deemed), it will continue to remain grandfathered with a reversionary nomination if the beneficiary is in receipt of an income support payment when the death benefit pension reverts to them.

5. With the introduction of the pension transfer cap of \$1.6m from 1 July 2017, death benefit pensions will be counted towards the recipient's pension transfer cap at commencement. This may become problematic when the beneficiary has already used (partly or fully) your pension transfer cap.

A modification applies to reversionary pensions, where the reversionary beneficiary has 12 months after the date of death before the pension counts towards your pension balance cap. This means the reversionary beneficiary will have time (12 months) to grieve and consider options available to them without having to pay penalty tax.

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