# 7. Superannuation

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## Summary

7.1 A significant proportion of the wealth of older people is held in superannuation funds.[1] Abuse of an older person may include the use of deception, threats or violence to coerce the person to contribute, withdraw or transfer superannuation funds for the benefit of the abuser. Abuse could also include making certain investment decisions that may advantage the abuser now or in the future. Other issues relating to possible elder abuse include questions about the ability of a person acting under a power of attorney to deal with superannuation.

7.2 Submissions to the ALRC generally identified fewer concerns with financial abuse in the context of superannuation than with respect to bank accounts and other financial assets. This may be because superannuation funds are subject to significant access controls. This was noted by the Financial Services Council:

> A rollover (when a person’s super fund is transferred to another super fund in their own personal name or to [a self-managed superannuation fund] where they are a

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1 Australian Bureau of Statistics, *Household Income and Wealth, Australia, 2013-14: Superannuation in Australia, 2003-04 to 2013-14, Cat No 6523.0* (2016).

> trustee) is subject to stringent checks by the superannuation fund where funds are withdrawn from;
>
> A transfer from a person's super fund to another person's super fund is only allowed in limited situations such as death or divorce, and in these events additional checks and paperwork is required; and
>
> A withdrawal can only be made once a condition of release is met and for most Australians, this means reaching their preservation age, and even in this circumstance, withdrawals can only be transferred to the superannuation trustee's nominated bank account.[2]

7.3 The ALRC did identify two particular areas of concern regarding potential elder abuse in the context of superannuation. The first relates to what are called 'binding death benefit nominations' (BDBNs). The second relates to self-managed superannuation funds (SMSFs) which are subject to less regulatory oversight than retail and industry superannuation funds. Potential for elder abuse in the context of pressure to make a BDBN may occur through two means: the exercise of influence to have the older person make, or alter, a death benefit nomination in the trusted person's favour; and seeking to make a death benefit nomination under the supposed authority of a power of attorney.

7.4 The ALRC considers that BDBNs should be seen to be 'will-like' in nature, and, from a policy perspective, treated similarly to wills. There is much uncertainty and ambiguity concerning BDBNs of superannuation funds, particularly whether an enduring attorney may sign a BDBN on behalf of a member. The ALRC has therefore concluded that these uncertainties and ambiguities need to be resolved in a focused review of the provisions to establish the clear ambit of the legislative provisions and their relationship to superannuation trust deeds. The central legal issue concerns the scope of the ability for fund members to direct trustees with respect to the payment of funds on the member's death—as a matter of the construction of the trust deed as affected by legislation—and the formal requirements that may be required to do so, under the deed or by regulation.

7.5 The regulatory framework for SMSFs was designed on the premise of self protection. Such a regulatory framework may be problematic, as a larger number of SMSFs come under the control of older people who may require increasing decision-making support. The ALRC's recommendations in relation to SMSFs are designed to:

- better facilitate the process for appointing a person's enduring attorney as trustee/director of their SMSF in the event of a legal disability;
- improve planning for a potential legal disability as part of the operating standards of an SMSF; and
- provide for Australian Taxation Office (ATO) notification where an enduring attorney has taken over as trustee/director of the SMSF following the principal suffering a legal disability.

2 Financial Services Council, *Submission 78*.

# Financial abuse and superannuation funds

## Regulation of superannuation

7.6 The Australian Prudential Regulation Authority (APRA) is the prudential regulator for superannuation funds, other than SMSFs. SMSFs operate without prudential controls and are supervised by the ATO.

7.7 The Australian Securities and Investments Commission (ASIC) is responsible for consumer protection with regard to superannuation. It is concerned with the relationship between superannuation trustees and consumers, and aims to ensure members receive proper disclosure, useful information, and can access complaint-handling procedures.

7.8 The Superannuation Complaints Tribunal (SCT) deals with complaints about the decisions and conduct of trustees of superannuation funds other than SMSFs.

## Examples of financial abuse

7.9 Stakeholders identified a diverse range of instances of financial abuse of older people through unauthorised access to superannuation funds.[3] ASIC highlighted a number of examples of potential financial elder abuse in the context of superannuation:

> instructions to take a portion of a superannuation benefit as a lump sum rather than a pension may as much reflect the importance to the elder fund member of paying down debt, or facilitating new accommodation arrangements as action by an abuser to access superannuation money for their own benefit.
>
> ... instructions to continue drawdown of only the statutory minimum amount of an account based pension may reflect the active management of the elder person's longevity risk, rather than maximising the value of a death benefit that may become payable to an abuser.
>
> ... instructions in relation to the part commutation of an elder person's account based pension may as much reflect the need to meet a 'lumpy expense', such as in relation to health care, as action by an abuser to access superannuation money for their own benefit.[4]

7.10 The link between financial abuse of superannuation and banking was described in a case study provided by the North Australian Aboriginal Legal Service:

> An older Aboriginal man, who had accessed his superannuation, had his bank card stolen by his daughter who went on to withdraw a substantial amount of money from his account.[5]

7.11 Another example was provided by the Public Trustee of Queensland, who gave the example of a daughter of an elderly person suffering dementia who was able to procure the signature of that adult to withdraw a large sum in three instalments from a fund:

> All that was required in order for the instruction to the fund to transfer money was a form apparently signed by the adult which in this case was emailed to the superannuation fund. As it happens the funds ultimately were dissipated by the daughter for her own benefit.[6]

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3 See, eg, FINSIA, *Submission 339*; Townsville Community Legal Service Inc, *Submission 141*; ASIC, *Submission 125*.

4 Australian Securities and Investments Commission, *Submission 125*.

5 North Australian Aboriginal Legal Service, *Submission 116*.

6 Public Trustee of Queensland, *Submission 249*.

7.12 The interaction between superannuation and powers of attorney in the context of elder abuse was demonstrated in the following case study provided by Advocare Inc (WA):

> Enid is an elder woman who nominated her daughter Cathy as her Enduring Attorney. Enid has tolerated financial abuse by Cathy for many years as she has no-one else to assist her with things she finds too difficult to do on her own. Cathy is now pressuring Enid to transfer superannuation funds into Cathy's bank account, claiming that Enid will get a better return on investment. Enid was advised not to sign anything but is still vulnerable as she chose not to revoke her EPA.[7]

7.13 A particular risk in the context of SMSFs was the potential need for trustees to have increasing decision-making support. The Financial Services Institute of Australasia (FINSIA) noted that:

> the issues of population ageing and cognitive decline are a 'silent tsunami' for self-managed super funds (SMSFs), exposing investors in this sector to financial abuse, including fraud and inappropriate investment advice.[8]

7.14 The Office of Public Guardian (Qld) (OPG) provided a case study that highlights the particular complexities that arise where a trustee loses decision-making ability. The case study concerned a man in his 80s named 'Peter':

> Among Peter's many financial assets was a self-managed superannuation fund (SMSF), of which Peter had been appointed director of the trustee company of the fund. A couple of years after moving into care, Peter was diagnosed with dementia, at which time Peter's attorneys, appointed under an enduring power of attorney, assumed control of Peter's financial affairs. A complaint was made to the OPG that the attorneys were financially mismanaging Peter's funds. Peter was aged in the late 80s at the time of the complaint.
>
> The [OPG] investigated the matter and identified … that the attorneys were not competent to manage Peter's financial affairs due to the complexity, and their lack of understanding of the laws regulating SMSFs.
>
> The investigation identified that, following Peter's loss of capacity to make decisions, no changes had been made to the SMSF and Peter remained the director of the trustee company. The accountant, who had managed the accounting for Peter's business for years, was transacting on the SMSF after Peter lost capacity. … The attorneys did not take any action to ensure that the SMSF was compliant after Peter lost capacity, and were allowing the accountant to make decisions in relation to the SMSF when he had no authority to do so.[9]

7.15 Recommendations in other chapters of this Report address financial abuse in the context of powers of attorney and banking. Those reforms would assist in addressing a number of these examples of financial abuse. This chapter focuses specifically on the issue of elder financial abuse in the context of BDBNs, and in the SMSF sector.

## Consistency in language about decision-making ability

7.16 Different language is used to describe the instances where a person does not have the decision-making ability to make legal decisions For example, the *Superannuation Industry (Supervision) Act 1993* (Cth) (*SIS Act*) uses the term 'legal disability' and the *Corporations Act 2001* (Cth) uses the term 'mental incapacity'. Moreover, legal capacity is defined in subtly different ways across the states and

7 Advocare Inc (WA), *Submission 86*.
8 Financial Services Institute of Australasia, *Submission 137*.
9 Office of the Public Guardian (Qld), *Submission 173*.

territories.[10] Differences in terminology can have practical consequences in terms of whether there is an authority to act. The ALRC has previously recommended that there be consistent terminology used for decision-making ability to provide consistency and certainty.[11]

# Death benefit nominations

## The legal framework

7.17 The payment of the superannuation funds of a member on the member's death is a matter that is determined by the governing rules of the superannuation fund. As a matter of trust law, a trustee is not able to delegate the exercise of their powers under the trust, except to the extent permitted under the trust instrument itself, or by virtue of legislation.[12] Similarly, as a general rule, the beneficiaries cannot direct the trustee how to exercise a discretionary power.[13]

7.18 Part 3 of the *SIS Act* prescribes operating standards for funds, including in relation to benefit payments.[14] The standards themselves are set out in the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (*SIS Regulations*). With respect to APRA-regulated superannuation funds or approved deposit funds—collectively referred to as superannuation entities—the payment standards are set out in pt 6 of the *SIS Regulations*, including in relation to payment on the death of a member.

7.19 As the relevant Australian Prudential Regulation 'Prudential Practice Guide' explains, there are five different death benefit arrangements, 'each with its own requirements and consequences':

> (a) automatic reversionary benefit (where trustee exercises no discretion);
>
> (b) non-binding nomination (where there is full trustee discretion);
>
> (c) binding nomination (under section 59(1A) of the *SIS Act*);
>
> (d) non-lapsing nomination (under section 59(1)(a) of the *SIS Act*); or
>
> (e) complete discretion of the trustee if none of these nominations has been made and the reversionary benefit is not applicable.[15]

7.20 Section 59(1A) of the *SIS Act* provides that the governing rules of a superannuation entity *may* require a trustee to provide any benefits in respect of the member on or after the member's death to the legal personal representative or a

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10 See ch 2.

11 See Australian Law Reform Commission, *Equality, Capacity and Disability in Commonwealth Laws*, Report No 124 (2014) ch 2.

12 *Halsbury's Laws of Australia*, Title 430, 'Trusts', (D) 'Trustees' Power to Delegate and Employ Agents', [430-4385] 'Duty not to delegate and exceptions'; JD Heydon and Mark Leeming, *Jacob's Law of Trusts in Australia* (LexisNexis Butterworths, 7th ed, 2006) [1723]. The rule is expressed in the Latin maxim '*delegatus non potest delegare*'.

13 *Halsbury's Laws of Australia*, Title 430, 'Trusts', (B) 'Exercise of Powers of Trustees', [430-4345] 'Influence of view of third parties on exercise of power'.

14 *Superannuation Industry (Supervision) Act 1993* (Cth) s 55A. This section provides that the governing rules of a regulated superannuation fund must not permit a fund member's benefits to be cashed after the member's death otherwise than in accordance with the prescribed standards.

15 Australian Prudential Regulation Authority, *Prudential Practice Guide: SPG 280—Payment Standards for Regulated Superannuation Funds and Approved Deposit Funds* (2012) [55].

dependant or dependants of the member, so long as the notice complies with any conditions contained in the *SIS Regulations*.[16]

7.21 Section 59(1A) of the *SIS Act* is an enabling provision and the governing rules of superannuation funds do commonly provide for funds held by a member to be paid on the person's death in accordance with a binding nomination of the member. The governing rules of the fund may, however, stipulate requirements that are more restrictive.[17] The section also does not exclusively cover the field in which a member can give a trustee a nomination.[18]

7.22 If the governing rules of a fund permit such a nomination, reg 6.17A(4) of the *SIS Regulations* states that the trustee *must* pay a benefit to the person or persons mentioned in the notice if the matters set out are complied with:

> (a) the person or each of the persons, mentioned in the notice is the legal personal representative or a dependant of the member; and
>
> (b) the proportion of the benefit that will be paid to that person, or to each of those persons, is certain or readily ascertainable from the notice; and
>
> (c) the notice is in accordance with subregulation (6); and
>
> (d) the notice is in effect.

7.23 The *SIS Act* defines 'legal personal representative' to mean 'the executor of the will or administrator of the estate of a deceased person, the trustee of the estate of a person under a legal disability or a person who holds an enduring power of attorney granted by a person'.[19] 'Dependant' in this context is defined as meaning the spouse of the person, any child of the person, and any person with whom the person has an interdependency relationship.[20] 'Spouse' is given an extended definition and includes same-sex and de facto relationships, registered or otherwise.[21] 'Interdependency relationship' is also defined as a close personal relationship of people who live together, where one or each of them provides the other financial support and one or each of them provides the other with domestic support and personal care.[22]

7.24 Regulation 6.17A(6) sets out the formal requirements for a nomination under reg 6.17(4). It must:

- be in writing;
- be signed and dated by the member in the presence of two witnesses, each of whom have turned 18, and neither of whom is mentioned in the nomination; and

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16 See *Halsbury's Laws of Australia*, Title 400, 'Superannuation', (8) 'Governing Rules of Superannuation Entities', [400-850] Non-delegable discretion. Section 59(1A) does not apply to SMSF: see *Munro v Munro* [2015] QSC 61 and accordingly an SMSF BDBN can last indefinitely.

17 Australian Prudential Regulation Authority, *Prudential Practice Guide: SPG 280—Payment Standards for Regulated Superannuation Funds and Approved Deposit Funds* (2012) [7].

18 *Retail Employees Superannuation Pty Ltd v Pain* [2016] SASC 12 (8 August 2016) [439] (Blue J).

19 *Superannuation Industry (Supervision) Act 1993* (Cth) s 10(1). Definition of 'legal personal representative'.

20 Ibid s 10(1) (definition of 'dependant'). For the purposes of taxation law a death benefit dependant has a different definition: see Australian Taxation Office, *APRA-Regulated Funds: Paying Superannuation Death Benefits* <https://www.ato.gov.au/super/apra-regulated-funds/paying-benefits/paying-superannuation-death-benefits/>.

21 *Superannuation Industry (Supervision) Act 1993* (Cth) s 10(1) (definition of 'spouse'). Importantly, there is no requirement for the relationship to be for two years in duration. The Act simply requires the couple to live together on a genuine domestic basis.

22 Ibid s 10A. The requirements are cumulative.

- contain a declaration signed and dated by the witness stating that the notice was signed by the member in their presence.[23]

7.25 The trustee is also required to give to the member 'information that the trustee reasonably believes the member reasonably needs for the purpose of understanding the right of that member to require the trustee to provide the benefits'.[24]

7.26 A notice under reg 6.17(4) ceases to have effect at the end of three years after the day it was signed, or a shorter period fixed by the governing rules,[25] but can be renewed, amended or revoked.[26]

7.27 To 'amend' or 'revoke' a notice, the member is required to provide a notice complying with reg 6.17A(6).[27] However, to 'confirm' a notice, a lower formal threshold is required.[28] To 'confirm' the notice, the member is only required to give the trustee 'a written notice, signed, and dated, by the member, to that effect'.

7.28 In addition to a binding death nomination, some superannuation funds also permit a member to make a non-lapsing binding death nomination. This nomination is made under s 59(1)(a) of the *SIS Act*. A non-lapsing binding death nomination may only be made if permitted by the trust deed and with the active consent of the trustee.

7.29 When a binding nomination lapses, the nomination becomes non-binding. In such a case, the trustee's discretion with respect to death benefits is governed by the fund rules:

> When the trustee's discretion is exercised, members of industry superannuation funds or their dependants may contest the distribution. They are sometimes successful. The tribunal then sets aside the trustee's decision and substitutes its own decision. The tribunal can also scrutinise the validity of a binding nomination and may substitute its own decision if it so decides.[29]

## Disputes

7.30 The SCT was established under the *Superannuation (Resolution of Complaints) Act 1993* (Cth) and deals with complaints about superannuation, excluding SMSFs. Such complaints include questions concerning death benefit nominations and the trustees' exercise of discretion in relation to nominations. As the Tribunal explains:

> Key issues that arise for trustees when dealing with death benefit distributions include who should be considered as potential beneficiaries of a deceased member's death benefit and, if there are competing claims made by a number of potential beneficiaries, what must be taken into account when assessing who should be paid the death benefit and in what proportion. These are often complex issues that require careful consideration of multiple factors such as the degree of dependency of the potential beneficiary on the deceased member and the role and purpose of superannuation.[30]

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23 *Superannuation Industry (Supervision) Regulations 1994* (Cth) reg 6.17A(6).
24 Ibid reg 6.17A(3).
25 Ibid reg 6.17A(7).This is subject to a trustee of the entity complying with any conditions contained in the regulations, and the member's notice being given in accordance with the regulations. See *Superannuation Industry (Supervision) Act 1993* (Cth) s 59(1A).
26 *Superannuation Industry (Supervision) Regulations 1994* (Cth) reg 6.17A(5).
27 Ibid reg 6.17A(5)(b).
28 Ibid reg 6.17A(5)(a).
29 Nicola Peart and Prue Vines, 'Will Substitutes in New Zealand and Australia' in Alexandra Braun and Anne Roethel (eds), *Passing Wealth on Death: The Phenomenon of Will-Substitutes from a Comparative Perspective* (Hart Publishing, 2016) 107, 122.
30 Superannuation Complaints Tribunal, *Key Considerations That Apply to Death Benefit Claims* (2006) 2.

7.31 The discretionary nature of the payment of death benefits in many cases gives rise to many complaints to the SCT.[31] The Tribunal reported that, between January and March 2017, complaints concerning the distribution of death benefits comprised the 'biggest single complaint category', amounting to 21.5% of complaints received.[32]

7.32 The Tribunal has produced a guide in relation to its procedures for dealing with such complaints.[33] Where a nomination is binding, the trustee has no discretion to override it.[34] A challenge may only be made, for example, on the basis of the validity of the nomination, including a lack of legal capacity.[35]

## The potential for abuse

7.33 BDBNs are often made in the context of broader estate planning and, in particular, a desire to ensure the most tax effective structure for succession.[36] The inclusion of BDBNs in estate planning is encouraged: if superannuation is not considered, 'the family members inevitably will end up in conflict'.[37]

7.34 BDBNs may also be used to limit or manage any potential claims on the deceased's estate. Where the member's funds are paid to a dependant pursuant to a BDBN, those funds do not form part of the member's estate.[38] In all states and territories, except New South Wales, such property is not available under family provision laws. If a member's superannuation death benefit is substantial, the ability to remove the funds from the operation of family provision laws gives a member significant control after death. By contrast, in New South Wales, superannuation death benefits may be classified as 'notional estate' and brought within the jurisdiction of the court for the purposes of making a family provision order.[39]

7.35 The nominations covered by reg 6.17A(4) can only be made to the legal personal representative or 'dependants'. A nomination to a dependant could potentially be made under pressure. Although the person nominated in the notice cannot be a witness, the range of 'dependants' is still quite wide. Given that, for example, there are indications that financial abuse is committed by adult children,[40] and these are within

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31 Australian Prudential Regulation Authority, *Prudential Practice Guide: SPG 280—Payment Standards for Regulated Superannuation Funds and Approved Deposit Funds* (2012) [61]. The Tribunal describes it as 'an emotionally fraught topic': 'Focus: Death Benefits', *SCT Quarterly* (Q1 2017) <www.Sct.Gov.Au/Newsletters/Sct-Quarterly-Q1-2017>.

32 'Focus: Death Benefits', *SCT Quarterly* (Q1 2017) <www.Sct.Gov.Au/Newsletters/Sct-Quarterly-Q1-2017>.

33 Superannuation Complaints Tribunal, *Key Considerations That Apply to Death Benefit Claims* (2006).

34 Ibid [124]; *Determination D15-16\112* [2016] SCTA 39 (17 March 2016) [42].

35 Eg, *Determination No D16-17\124* [2017] SCTA 13 (25 January 2017); *Determination D15-16\112* [2016] SCTA 39 (17 March 2016); *Determination D14-15\172* [2015] SCTA 31 (2 March 2015).

36 See Australian Taxation Office, above n 20.

37 Caroline Harley, 'Supercharging Battles over Superannuation Death Benefits' (August 2014) *Law Society Journal* 68, 69.

38 *Williams v Federal Commissioner of Taxation* 81 CLR 359; *Re Danish Bacon Co Ltd Staff Pension Fund Trusts* [1971] 1 WLR 248; *McFadden v Public Trustee (Vic)* [1981] 1 NSWLR 15; *Baird v Baird* [1990] 2 AC 548. See, eg, Gino Dal Pont and Ken Mackie, *Law of Succession* (LexisNexis Butterworths, 2013) [20.3]; Rosalind Croucher and Prue Vines, *Succession: Families, Property and Death* (LexisNexis Butterworths, 4th ed, 2013) [3.10]–[3.12].

39 The notional estate provisions are discussed in Dal Pont and Mackie, above n 38, [20.57]–[20.76]. One commentator suggests that there may be a conflict between the *SIS Act*, as a Commonwealth law, allowing a member to nominate a recipient of superannuation, and the New South Wales provisions permitting the designation of that same benefit as 'notional estate' for family provision purposes, and that this 'could bring into play s 109 of the *Constitution* under which the Commonwealth law must prevail': Thomson Reuters, *The Laws of Australia* Title 36, 'Wills and Estate Administration', 36.2 'Family Provision' [36.2.730]. This statement is not supported by authority, nor has it been tested.

40 Rae Kaspiew, Rachel Carson and Helen Rhoades, 'Elder Abuse: Understanding Issues, Frameworks and Responses' (Research Report 35, Australian Institute of Family Studies, 2016).

the set of 'dependants' in the context of death benefit nominations, there is potential for contrivance for a nomination preferring a child—so long as there was a separate witness to satisfy reg 6.17A(6).

7.36 Similar pressure may be imposed to encourage a nomination to the estate so that the superannuation funds form part of the estate of the deceased to be governed by their will or intestacy.

7.37 The Law Council of Australia commented that, given the value of many members' death benefits, 'there is an unfortunate incentive to manipulate a member's nomination'.[41] State Trustees Victoria described as 'insidious', 'where a third party manipulates a person into nominating them as a binding death benefit nominee':

> It is unclear to what extent this happens but it should be considered a potential issue to be managed. Given that the binding death benefit nomination only takes effect after the death of the principal, disproving that the nomination was not valid would be very difficult.[42]

7.38 Pressure to make a will may also include pressure to make a binding death benefit nomination, as evident in a case study provided by the Queensland Law Society (QLS). A woman in her 70s, 'V', attended the office of the relevant law firm, brought by her 'partner' to make a will. The firm considered that V did not have legal capacity to make a will. It became apparent that there was also a superannuation nomination involved and the firm was concerned as to possible abuse of 'V' to make it:

> it became apparent through our discussions that V had made a binding death benefit nomination in relation to her superannuation to her 'partner'. Her superannuation, as far as we could tell was her largest asset. V had a copy of the nomination with her (given to her by her partner to bring into our meeting). The nomination had been made within the two weeks prior to our meeting. This concerned me as although the capacity to make a binding death benefit nomination is the ability to enter into a contract, and not the same as making a will, it was doubtful that V had the capacity to understand the nature and effect of that decision. Further it was probable that she was told to sign the nomination by her partner in front of the two witnesses.[43]

## Clarifying and reviewing the law

**Recommendation 7–1** The structure and drafting of the provisions relating to death benefit nominations in ss 58 and 59 of the *Superannuation Industry (Supervision) Act 1993* (Cth) and reg 6.17A of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) should be reviewed. The review should consider:

(a) witnessing requirements for making, amending and revoking nominations;

(b) the authority of a person who holds an enduring power of attorney in relation to the making, alteration and revocation of a nomination;

(c) whether a procedure for the approval of a nomination on behalf of a member should be introduced; and

(d) the extent to which other aspects of wills law may be relevant.

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41 Law Council, *Submission 61*.
42 State Trustees Victoria, *Submission 138*.
43 Queensland Law Society, *Submission 159*.

7.39 Recommendation 7–1 tackles a key problem in relation to BDBNs, namely the uncertainties and ambiguities that arise in the construction of ss 58 and 59 of the *SIS Act* and reg 6.17A of the *SIS Regulations*. The wider context concerns the equitable rules about trusts, and the extent to which beneficiaries can direct trustees in the exercise of their powers, through express provision in the trust deed and/or as authorised or required by legislation.

7.40 In the 2016 decision, *Retail Employees Superannuation Pty Ltd v Pain*, Blue J identified the problems in relation to the existing provisions and suggested that it was 'highly desirable' that the particular provisions 'be reviewed by the Commonwealth and recast'.[44] In particular, Blue J identified ambiguities as to which aspects of reg 6.17A of were prescriptive for a notice to pay a benefit to be effective.[45] Blue J referred to the 'strong desire by members of superannuation funds to be able to make non-lapsing nominations', but said that it was 'a question of policy whether and on what terms binding nominations are permitted and this is exclusively a matter for the Commonwealth Parliament and the Commonwealth Government'.[46] He considered that there were several 'policy options':

> One policy option would be to leave binding nominations to be governed exclusively by the governing rules of the superannuation fund, largely equating the position to that applying to wills under the general law in which (subject only to implied revocation on marriage) a will operates indefinitely until revoked. Another policy option would be to permit indefinite nominations subject to legislated manner and form requirements to ensure that a nomination is intended to be made by a member on an informed basis. Another option would be to provide that all indefinite nominations lapse on the occurrence of a legislatively defined event or events (such as marriage). Another option would be to provide that all nominations lapse on the effluxion of a legislatively defined period of time. Whichever policy option is adopted, it is desirable that it be a simple universal rule applying to all binding nominations as opposed to the current situation involving multiple alternatives adopted by superannuation fund trustees to permit their members to make fixed term or indefinite binding nominations in compliance with the legislation.[47]

7.41 The ALRC considers that such ambiguities need to be resolved in order to include consideration of the specific matters raised in the Discussion Paper and in this chapter.

7.42 The ability to make a BDBN, like the ability to make a will, is a key aspect of advance planning and an exercise of autonomy by older people and fund members generally. Both the language and types of nominations vary greatly. The expanding scope and value of superannuation means that clarity in understanding from the perspective of fund members and trustees is important.

7.43 Recommendation 7–1 adopts Blue J's suggestion for a review. Once the review is completed, improving the understanding of financial advisers and lawyers, as well as the information provided to superannuation fund members can be developed.

7.44 The review could be conducted by the Treasury as the Australian Government agency responsible for advising on broad features of retirement income policy,

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44 *Retail Employees Superannuation Pty Ltd v Pain* [2016] SASC 12 (8 August 2016) [512].
45 Ibid [495]–[496].
46 Ibid [513].
47 Ibid [514].

including the objectives, adequacy and overarching framework and design of the superannuation system.[48]

7.45 The review should include key government agencies, such as the APRA, the ASIC and the ATO. It should also include key stakeholder groups, such as: the Law Council of Australia; the Financial Planning Association of Australia; CPA Australia; and consumer groups, such as the SMSF Association (SMSFA), the Combined Pensioners and Superannuants Association and the Association of Independent Retirees.

## Reducing elder abuse

7.46 The ALRC considers that a number of strategies need to be adopted to assist in combating potential abuse. One is to ensure that the information that members are given about their rights in relation to BDBNs is clear. Another is to ensure that the advisers who are likely to be involved in the preparation of BDBNs are alert to the issues of potential abuse. Another is to consider other integrity measures, such as witnessing, to support the person in the exercise of their choice.

### *Information for members*

7.47 Regulation 6.17A(3) of the *SIS Regulations* provides that the trustee must give to the member information 'that the trustee reasonably believes the member reasonably needs for the purpose of understanding the right of that member to require the trustee to provide the benefits'.

7.48 An area of confusion that would benefit from clarification is the extent to which a nomination is 'binding' in the sense of being lapsing or not. As one solicitor commented:

> It is more important for a person making a death nomination to have the assurance that the nomination is binding and that it will continue to be binding even should they lose capacity. A binding nomination should therefore be binding unless expressly revoked or, at the very least, the principal must have the option to make a non-lapsing binding nomination.[49]

7.49 The clarification of the law, pursuant to Recommendation 7–1, will provide a firmer foundation for advice by trustees to members as required by reg 6.17A(3), and for the information that is provided through other avenues, such as the SCT. Websites of superannuation funds and the Tribunal may be for many people the natural first port of call in relation to locating information about death benefit nominations.

7.50 The approach to improving the provision of information to members needs to be multi-faceted and include recognition of the role of financial advisers, who are often involved in the process of assisting a member. Hamilton Blackstone Lawyers pointed to the 'crucial role' of a financial adviser in this situation:

> in a large proportion of cases where a person has a relationship with a financial adviser, binding death benefit nominations are completed following the provision of advice by that adviser. Furthermore, advisers generally assist in the completion and execution of binding death benefit nominations. It is critical that this continues to be the case.[50]

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48 The Treasury (Cth), 'Superannuation and Retirement' <www.Treasury.Gov.Au/Policy-Topics/SuperannuationAndRetirement>'.

49 T Chapman, *Submission 268*.

50 Hamilton Blackstone Lawyers, *Submission 270*.

7.51 The Financial Planning Association of Australia commented similarly, saying that a financial planner is more important than a lawyer in this context:

> Estate planning and superannuation are core subject areas in financial planning degrees and the Certified Planner Certification Program. Estate planning is not a core requirement of law degrees or Continuing Professional Development programs for legal practitioners.
>
> While a person is permitted to make a binding death benefit nomination without involving a solicitor, Australians who seek financial advice usually establish binding death benefit arrangements with the assistance of their professional financial planner.[51]

7.52 The SMSFA expressed a concern with respect to SMSFs, suggesting that SMSF advisers have 'death benefit nomination templates' which are used with their clients:

> This is a grey area with both accountants and financial planners providing these documents to client perhaps inappropriately and without expertise. In this regard there may be merit in placing the emphasis of death benefit nominations as part of an estate planning specialist process, as wills are. Greater awareness and education as to the legal risks around poorly constructed and executed BDBNs may encourage more SMSF trustees and their advisors to seek legal advice on BDBNs (and reversionary pensions).[52]

7.53 Given the key role that financial planners play in relation to superannuation advice, improving their understanding of the way that pressure to make or amend BDBNs may be brought to bear on older people is one strategy for combating elder abuse.

### *Witnessing*

7.54 The ALRC Discussion Paper included a proposal that the witnessing requirements for BDBNs should be equivalent to those for wills.[53] This was supported by stakeholders. For example, the Institute of Legal Executives (Victoria) commented that '[w]e strongly agree that these should be executed in the same manner as Wills, being an essential part of the estate plan'.[54]

7.55 The requirements in relation to witnessing for BDBNs are set out in reg 6.17A. As noted above, reg 6.17A(6) of the *SIS Regulations* requires that the notice making a BDBN must be signed by the member in the presence of two witnesses. The witnesses must be at least 18 years old and neither can be a nominee of the funds. The BDBN must also contain a declaration signed and dated by the witnesses that the notice was signed by the member in their presence.

7.56 These requirements are similar to wills and perform an analogous function. The witnessing requirements for wills are found in state and territory legislation, the essential elements of which are that there be two witnesses present at the same time and that what they are witnessing is the testator's signature, or the acknowledgment by the testator of their signature.[55] The requirement in reg 6.17A(6)(b)(ii) of the *SIS*

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51 Financial Planning Association of Australia (FPA), *Submission 295*.

52 SMSF Association, *Submission 382*.

53 Australian Law Reform Commission, *Elder Abuse*, Discussion Paper 83 (2016) prop 9–2.

54 Institute of Legal Executives (Vic), *Submission 320*. See also Seniors Rights Victoria, *Submission 383*; Law Society of South Australia, *Submission 381*; Chartered Accountants Australia and New Zealand, *Submission 368*.

55 Except in the ACT and Western Australia, it is no longer necessary for the witnesses to sign in the presence of each other: see summary in Croucher and Vines, above n 38, [7.17]; Dal Pont and Mackie, above n 38, [4.12]–[4.16].

*Regulations* that the witness not be a person ‘mentioned’ in the notice is similar to the witness-beneficiary rule for wills,[56] although given the modification of the latter rule, the regulation is stricter. Where the witness-beneficiary rule avoids the gift to the beneficiary, a failure to satisfy reg 6.17A(6)(b)(ii) would be a ground of invalidity of the notice. The Law Council of Australia observed that the validity of the nomination is an issue that regularly arises in relation to death benefit nominations.[57]

7.57 The formal requirements of reg 6.17A(6) may also be considered to be more stringent than wills. For example, unlike in relation to wills, there is no ‘dispensing power’ to forgive non-compliance with formalities.[58] In the context of wills, such matters are only raised post-mortem as part of the probate process. In the context of BDBNs, the ALRC does not suggest that similar powers should be introduced. The trustees of the fund may have an opportunity to identify issues of non-compliance with formal requirements during the member’s lifetime, though it may not become clear until the person’s death that a nominated dependant is in fact not a dependant.[59]

7.58 Several stakeholders suggested that the witnessing process could be made stricter. State Trustees Victoria, for example, suggested that the risk of misuse of BDBNs could be minimised by requiring there be witnesses ‘to verify that the person appeared to have capacity when the nomination was made’.[60]

7.59 Another suggestion was to require independent legal advice. The QLS, for example, suggested this, ‘[g]iven the ease with which binding death benefit nominations can be made and the risk to that asset’.[61] Law firm, Carroll & O’Dea, also suggested that ‘it might be worthwhile to require a member to obtain a certificate of independent legal advice prior to making a superannuation death benefit nomination’, but noted a number of questions relevant to this:

> What would the legal advice entail?
>
> Would this advice be required each and every time a member completes a death benefit nomination?
>
> What would be the effect if a member failed to obtain legal advice?[62]

7.60 The Law Council of Australia also noted that lapsing BDBNs may not necessarily need to be treated the same as non-lapsing nominations. In this context the Council did not support a requirement of independent legal advice:

> given that the provision of a certificate for superannuation nominations would mean that every time a person made a nomination (some retail funds require a nomination every three years) with respect to his or her superannuation it would be necessary to see a lawyer.[63]

7.61 The Law Council of Australia commented that, while solicitors are often involved with the preparation of wills, this is much less the case in the preparation of

56 See ch 8.
57 Law Council, *Submission 61*.
58 On dispensing powers in relation to wills, see Croucher and Vines, above n 38, ch 8; Dal Pont and Mackie, above n 38, [4.30]–[4.47].
59 In the event that a notice is found to be invalid, the funds would be paid at the discretion of the trustee.
60 State Trustees Victoria, *Submission 138*.
61 Queensland Law Society, *Submission 159*.
62 Carroll & O’Dea, *Submission 335*.
63 Law Council, *Submission 351*.

nominations. Abuse could be reduced 'if a solicitor is involved and the direction of the death benefit is to the estate'.[64]

7.62 Even if witnessing were made stricter, Rodney Lewis observed, from cases involving wills, that 'important witness evidence routinely comes from the solicitor who prepared it, the medical practitioners who have attended the testator, the friends and relatives who have been in contact with the person before the signing of the document'.[65]

7.63 In its 2013 *Succession Laws* Report, the Victorian Law Reform Commission explored other integrity measures for witnesses directed towards protecting 'older and vulnerable will-makers from undue influence by potential beneficiaries or others'. Two specific measures were explored: requiring a witness to certify that the will-maker had the necessary mental capacity to sign their will, and signed the will freely and voluntarily; and requiring a medical practitioner to witness and assess the person's capacity and freedom of will. Neither was adopted as a recommendation.[66]

7.64 The ALRC considers that the witnessing requirements of reg 6.17A(6) are set at an appropriately high level to act as a validating measure for a BDBN, similar to that performed for wills. Witnesses to wills are only required to attest that the testator signed the will in their presence. The ALRC concludes that adding witnessing requirements to the making of a BDBN is unnecessary. Obtaining full and independent advice about such matters may be constructive as part of best practice estate planning, but it would be unduly burdensome to add the requirement of independent legal advice to the making of a BDBN. Improving the understanding of financial advisers and lawyers about the dynamics of elder abuse and the ways that this may present in the context of pressure to make or change advance planning instruments is a supportive approach and part of wider strategies to combat elder abuse. Financial advisers and lawyers also need to be sensitive to issues of impaired decision-making ability and how best to support clients in such cases.

7.65 The ALRC notes that the formal requirements for confirmation of a nomination are set at a lower level than for making, amending or revoking a nomination. This is tied up with the issue about lapsing nominations. As a matter of policy, however, this is an area where the formal threshold is lower and therefore consideration of this difference would be an appropriate matter to be analysed as part of the review in Recommendation 7–1.

## Death benefit nominations and substitute decision makers

7.66 Specific matters that need to be considered in the recommended review are discussed below.

### *Should enduring attorneys be able to make BDBNs?*

7.67 In the Discussion Paper, the ALRC proposed that donees of enduring powers of attorney should not be able to make a BDBN on behalf of a member. The legal position on this issue was considered briefly in the ALRC Report, *Equality, Capacity and Disability in Commonwealth Laws*,[67] where it was pointed out that, as a matter of law,

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64 Law Council, *Submission 61*. With respect to capacity issues, the Law Council of Australia referred to *D14-15\172* [2015] SCTA 31.

65 R Lewis, *Submission 349*.

66 Victorian Law Reform Commission, *Succession Laws*, Report (2013) [2.19]–[2.26].

67 Australian Law Reform Commission, *Equality, Capacity and Disability in Commonwealth Laws*, Report No 124 (2014) [11.55]–[11.65].

there does not appear to be any restriction in the *SIS Act* or *SIS Regulations* that would prevent a person acting under a power of attorney from completing and signing a BDBN.

7.68 In *Determination D07–08\030*, the SCT stated that, in principle, an enduring power of attorney would permit an attorney to complete and sign a BDBN on behalf of the member. As the Tribunal did not decide the matter on the basis of the binding nomination, however, its comments are not of direct application. Hence, the Law Council of Australia observed that '[w]hether the scope of an attorney's authority extends to making a nomination remains a matter of debate'.[68]

7.69 In the *Equality, Capacity and Disability* Inquiry, the Law Council of Australia pointed to the different practices of funds:

> some funds accept a nomination by a person holding an enduring power of attorney granted by the member, generally without inquiring as to the wishes of the member. Some funds do not accept a nomination by a person holding an enduring power of attorney, with the result that binding nominations cannot be made by these members.[69]

7.70 The Law Council of Australia suggested that superannuation funds would adopt a more consistent approach if there were greater clarity in legislative provisions governing superannuation death benefits.[70]

7.71 As explained in the *Equality, Capacity and Disability* Report, the policy issue is a difficult one, given the difference between a nomination, as a lifetime act, and its effect, which is will-like in nature—as it affects property after the death of the member. The Law Council of Australia agreed with the ALRC that the main issue concerning BDBNs is that there is currently no clear policy position on whether a nomination should be considered similar to a will or simply a lifetime instruction in relation to a person's assets. The Council also agreed with the ALRC's analysis that nominations are will-like in nature and they should be treated in policy terms 'similarly to wills'.[71]

7.72 In this Inquiry, the ALRC focused on this issue again and proposed that the *SIS Act* and *SIS Regulations* 'should make it clear that a person appointed under an enduring power of attorney cannot make a binding death benefit nomination on behalf of a member'.[72]

7.73 The ALRC acknowledges that the proposal to prohibit an attorney, acting under an enduring power, from making a BDBN does raise policy challenges in the context of the three-year limit on nominations under reg 6.17A(7).[73]

7.74 For example, a member may make a BDBN and then subsequently lose legal capacity. If the attorney does not have the power to renew the BDBN when it lapses after three years, the principal's superannuation funds may be distributed:

- in a way that the member had not intended;

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68 Law Council, *Submission 61*.

69 Quoted in Australian Law Reform Commission, *Equality, Capacity and Disability in Commonwealth Laws*, Report No 124 (2014) [11.60].

70 Ibid [11.60].

71 Ibid [11.63], citing Law Council *Submission 142*.

72 Australian Law Reform Commission, *Elder Abuse*, Discussion Paper 83 (2016) prop 9–3.

73 *Superannuation Industry (Supervision) Act 1993* (Cth) s 59(1A); *Superannuation Industry (Supervision) Regulations 1994* (Cth) reg 6.17A.

- in a manner less ideal for tax purposes when compared with the lapsed binding death nomination; or
- in a manner that results in the funds forming part of the estate of the member which may be subject to certain creditors' claims.[74]

7.75 A number of stakeholders provided very informed submissions on the matter of BDBNs: the Law Council of Australia, several law firms, financial planners and chartered accountants. With respect to the existing position in relation to BDBNs, a common point was that the *making* of a BDBN should be seen as different from the *renewal* of a BDBN. In this context there is a problem of the '*lapsing* binding death benefit nomination'. Reg 6.17A states that a notice under 6.17A(4) ceases to have effect after three years. But there can also be 'non-lapsing binding death benefit nominations', if superannuation fund rules permit them.

7.76 Where BDBNs lapse, a specific policy issue is whether a person who is an attorney under an enduring power, should be able to *confirm* the nomination so that it continues to have validity—that this is different from making a BDBN and it continues the autonomous choice of the member. Where there is *no* BDBN there are two distinct issues: the legal issue of whether a person who is an attorney under power *can* make a nomination in exercise of that power; and the policy issue of whether they *should* be able to do so.

7.77 Richard Williams and Brian Herd explain that the legal issue contains several sub-questions. First, the issue needs to be considered under state and territory enduring powers of attorney (EPOA) legislation—for example, whether a power in relation to 'financial affairs' encompasses the making of a BDBN; and, secondly, under the specific terms of the instrument of appointment itself. Further, the attorney under power, as a fiduciary, would be subject to restrictions as a matter of law on the way any such power may be exercised. Hence, as Williams and Herd conclude:

> Even if an attorney under an EPOA has a sufficiently wide scope of authority to act on behalf of their principal in respect of superannuation, the provision by the attorney of a notice to a superannuation trustee that would have the effect of conferring a benefit on the attorney, or increasing the value of such benefit would (absent any special condition to the contrary) clearly amount to a breach of the attorney's duties. The revocation of an existing nomination, in order to increase the likelihood of a trustee making payment of a death benefit to the member's legal personal representatives, in circumstances where the attorney is a beneficiary under the member's will or on intestacy, would give rise to the same issue.[75]

7.78 A separate issue is the extent to which superannuation laws allow for this. As Williams and Herd explain, reg 6.17A stipulates two distinct acts to be done by a member: the signature of the notice by the member, and the giving of the notice to the trustee. While they suggest that 'it is arguable that the acts of signature and of giving the notice are capable of being performed by an attorney', the matter is not 'beyond doubt'.[76] Carroll & O'Dea said, similarly, that the question of whether an attorney's authority extends to making a nomination 'remains a matter of debate'.[77] Hamilton

74 Superannuation funds are protected in part by s 116(2)(d) of the *Bankruptcy Act 1966* (Cth). Keeping the superannuation death benefit out of the estate by paying directly to a beneficiary may increase protections against creditor claims.

75 Richard Williams and Brian Herd, 'An Enduring Question: To What Extent Can Those Appointed under an Enduring Power of Attorney in Australia Make, Revoke, Alter or Confirm a Superannuation Death Benefit Nomination?' [2015] (March) *STEP Journal* 18, 25.

76 Ibid 27.

77 Carroll & O'Dea, *Submission 335*.

Blackstone Lawyers stated their view that the *SIS Act* and *SIS Regulations* 'already do not permit attorneys to make binding death nominations on behalf of the principal' and welcomed 'the opportunity for further clarity to be provided on this aspect'.[78]

7.79 Williams and Herd also note the difference in the requirements of making and confirming a nomination and suggest that:

> This may explain why some practitioners suggest that an attorney under an EPOA may renew a nomination, but not make, revoke or alter a nomination. In the absence of any express statement to that effect in the legislation, that view does not appear to be sufficiently supported by the terms of regulation 6.17A itself.[79]

7.80 Carroll & O'Dea commented that 'superannuation funds would adopt a more consistent approach if there were greater clarity in legislative provisions governing superannuation death benefits'.[80] Uncertainty is 'undesirable', and is 'a peculiarity that needs resolution', because, as Williams and Herd conclude:

> For many persons, a binding death benefit nomination will form an integral part of their estate planning, as it should ensure (or, at least, increase the likelihood) that the relevant assets pass as the member intends.[81]

7.81 In the Discussion Paper, the ALRC expressed the policy position that an attorney should not be able make a BDBN on behalf of a member and that the legislative uncertainty should be clarified in line with this. This was based on the analogy made between BDBNs and wills and, as wills can only be made by a person with legal capacity, the ALRC concluded that a person holding an enduring power of attorney should not be able to sign a binding death benefit nomination on behalf of the member. As the role of an enduring attorney is one focused on the lifetime transactions and needs of the person, a point also emphasised in the submission of law firm Carroll & O'Dea,[82] the ALRC concluded that it was not appropriate for such a person to make a binding death benefit nomination that was will-like in effect.

7.82 The Law Council of Australia was concerned about the lack of clarity as to whether an attorney's power extended to the making of a BDBN and considered that it would be desirable if the *SIS Act* and *SIS Regulations* were amended to make clear 'that a person appointed under an enduring power of attorney cannot make (confirm, amend or revoke) a BDBN (or a non-lapsing nomination or a non-binding nomination) on behalf of a member'. However the Law Council of Australia stated an exception: 'unless this is expressly authorised in the document by specific reference to the making of BDBNs (or other nominations)':

> At present this is an area of significant confusion for superannuation funds, with some funds allowing the holder of an enduring power of attorney to make, amend or revoke a BDBN, and other funds not allowing this. The issue has not been tested before the Courts. Conflict issues also commonly arise, where the holder of the enduring power of attorney is an individual who would benefit from the making, amendment or revocation of a BDBN. Such issues can be addressed by the inclusion of specific authorising provisions in the relevant power of attorney, but there may then be further complexity with the correct drafting of such documents. In any event, the authorisation should be express, and should include the ability to nominate the

78 Hamilton Blackstone Lawyers, *Submission 270*.
79 Williams and Herd, above n 75, 27.
80 Carroll & O'Dea, *Submission 335*.
81 Williams and Herd, above n 75, 27, 28.
82 Carroll & O'Dea, *Submission 335*.

attorney themselves and to amend the BDBN (or other nomination) in their own favour if this is desired by the member.[83]

7.83 The issue of express authorisation was also raised by the Financial Services Council, which said that a person under an EPOA should only be able to make or renew a BDBN on behalf of a member if expressly authorised by the EPOA.[84] Chartered Accountants Australia and New Zealand made a similar comment, but added: ‘we would also include a person appointed under a general power of attorney in this prohibition unless the power the power had been specifically granted’.[85]

7.84 The issue of express authorisation in an enduring power of attorney is a matter that should be considered as part of the review set out in Recommendation 7–1. While the ALRC expresses a policy position against a person under an EPOA being able to make a nomination on behalf of the member, the ALRC did not consider the question of express authorisation in the EPOA itself. This is a matter that may require more investigation. For example, the ALRC also proposes that a process for approval of a nomination be considered as part of the recommended review.

7.85 A similar issue may be raised in relation to someone appointed by a tribunal as a financial administrator of a person who has lost, or who has diminished, decision-making ability.[86] If a financial administrator is given wide powers in relation to financial matters, then the analysis of this chapter may also apply to a financial administrator in such a case.[87]

7.86 The ALRC also acknowledges that the policy question, however, is a wider one and needs to address not only whether an attorney under an EPOA, or a financial administrator appointed with respect to a person’s financial affairs, should be able to make a nomination, but also the other situations addressed in reg 6.17A: namely, concerning confirming, altering and revoking a nomination.[88]

### *Responding to changes in circumstances*

7.87 Certain aspects of wills law are directed towards changes in circumstances of testators. First, a will is revoked automatically in certain circumstances. Secondly, there is a process of seeking court approval for a will for a person who does not have testamentary capacity.

7.88 It is a longstanding rule that, as a matter of law, wills are revoked on marriage. In the latter part of the twentieth century this was extended to revocation on dissolution of marriage.[89] Given the analogy drawn between BDBNs, especially those that are non-lapsing, and wills, the ALRC considers that a review of the BDBN provisions should be a broad one and include consideration of such doctrines.

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83 Law Council, *Submission 351*.

84 Financial Services Council, *Submission 359*. Similarly: SMSF Association, *Submission 382*.

85 Chartered Accountants Australia and New Zealand, *Submission 368*.

86 See ch 10.

87 The definition of ‘legal personal representative’ includes a person holding an enduring power of attorney, but does not refer to an appointed financial administrator: *Superannuation Industry (Supervision) Act 1993* (Cth) s 10(1).

88 A further issue concerns the non-renewal of a BDBN: if an attorney under an EPOA is able to make a nomination, the attorney may also choose not to do so, which may have beneficial consequences for the attorney or the attorney’s family members pursuant to the will or intestacy of the fund member.

89 See Croucher and Vines, above n 38, [9.2]–[9.9]; Dal Pont and Mackie, above n 38, [5.23]–[5.41].

7.89 A concern to be able to respond to changes in circumstances in the superannuation context was raised by stakeholders.[90] Hamilton Blackstone Lawyers suggested that the *non-lapsing* death benefit nominations, offered by many superannuation funds, provided flexibility to deal with changes in circumstances, 'in that the trustee of the superannuation fund can exercise its discretion to withdraw its consent to the nomination if the member's circumstances have changed'.[91] The ALRC acknowledges that, while this is one mechanism for responding to changes in circumstances, it puts matters in the hands of the trustees to honour, or not, the wishes as expressed in the nomination. The alternative, as in the case of wills, is to revoke the nomination in such a case, allowing for a new nomination to be made to reflect the change in circumstances. The ALRC considers that such similarities and differences are best considered in a full review.

7.90 The Public Trustee of Queensland referred to experience in acting as administrator for adults with impaired decision-making ability and suggested that attorneys should have the power to make a BDBN, for example where:

> Circumstances have changed such that it is demonstrably clear that an existing binding nomination should be changed, or effectively withdrawn (for example a binding nomination to a spouse where the relationship has ended).[92]

7.91 The need to renew a nomination that lapses, after a person loses capacity, was a concern for the Senior Rights Service (SRS) in light of the person's 'estate planning requirements'.[93] SRS was concerned that other protections were needed in such a case. The Financial Planning Association gave another example:

> For example, if the principal had not disclosed to his children the existence of a sibling, and the family wanted to treat the newly found child equally. Exceptions to the prohibition should apply under a court order in certain circumstances.[94]

7.92 The ALRC considers that changes in circumstances can be addressed in two ways, both based on analogy from wills laws. The Law Council of Australia, for example, suggested that revocation 'in the same circumstances that a will would be revoked' should be considered.[95] The other way wills law responds to changes in circumstances, and particularly a loss of legal capacity, is through a process of approval known as 'statutory wills'.

7.93 A basic principle of wills formalities is that a person is required to have testamentary capacity when making a will. If a person was regarded as no longer having testamentary capacity, any will made by such person would be void.[96] Now, however, under strict conditions, wills can be authorised by the court in all states and territories where a person is regarded as having lost, or never having had, legal capacity.[97] In the succession context it is a relatively new jurisdiction for the court to

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90 See, eg, Seniors Rights Service, *Submission 296*; Financial Planning Association of Australia (FPA), *Submission 295*; Hamilton Blackstone Lawyers, *Submission 270*.

91 Hamilton Blackstone Lawyers, *Submission 270*.

92 Public Trustee of Queensland, *Submission 249*.

93 Seniors Rights Service, *Submission 296*. See also Institute of Legal Executives (Vic), *Submission 320*.

94 Financial Planning Association of Australia (FPA), *Submission 295*.

95 Law Council, *Submission 351*.

96 See, eg, Croucher and Vines, above n 38, ch 6.

97 *Succession Act 2006* (NSW) ss 18–26; *Succession Act 1981* (Qld) ss 21–28; *Wills Act 1936* (SA) s 7; *Wills Act 2008* (Tas) ss 21–28; *Wills Act 1997* (Vic) ss 21–30; *Wills Act 1970* (WA) s 40; *Wills Act 1968* (ACT) ss 16A–16I; *Wills Act 2000* (NT) ss 19–26.

be able to approve these ‘statutory wills’. It is exercised cautiously, given the importance accorded to testamentary freedom as a valued property right.[98]

7.94 There may be an opportunity to consider an analogous process in relation to BDBNs, as part of the broader considerations about how such nominations operate. Such an approach could sit alongside the policy position that an attorney under an enduring power, by virtue of that power alone, should not be able to make a BDBN for a member of a superannuation fund.

7.95 If a member dies, then any superannuation balance is paid in accordance with the rules of the fund. That balance may well form part of the member’s estate in due course. A person who holds an enduring power of attorney may apply for a statutory will on behalf of the member during the member’s lifetime, but that is an entirely different matter from seeking to use the power of attorney to make the death benefit nomination on behalf of the member. The application for a statutory will would be subject to the strict scrutiny of the court. Whether the authorisation of a court should be required, or some other analogous process, is a matter for consideration in the review recommended in Recommendation 7–1.

7.96 The Law Council of Australia agreed that there should be ‘a cost effective way for an attorney to make an application to a tribunal to authorise a change in the principals’ affairs in certain circumstances’ and supported consideration of a process of court approval as part of the ‘consideration of the broader consequences’ if attorneys under EPOAs were not allowed to act in relation to BDBNs:

> In the absence of such provisions, individuals who lose capacity will be at risk of having no BDBN in place (given that generally a BDBN in a fund, other than a self-managed superannuation fund, will lapse after 3 years unless a mechanism is adopted for non-lapsing nominations or reversionary pension rules apply).
>
> Perhaps more importantly, individuals will be at risk of having a BDBN that has become inappropriate continue in effect until lapsing.
>
> Clearly, it would be desirable that the Court should have the ability to consider these circumstances and whether it should intervene to revoke, amend or re-make a BDBN to avoid an outcome that would not have aligned with the member’s intentions had they had capacity.[99]

7.97 The Law Society of South Australia also supported an approval process for a nomination put forward by an attorney under an EPOA ‘where the consent of the Tribunal has been obtained’:

> This would offer the opportunity to deal with circumstances where a non-lapsing binding nomination has been put in place by a donor of a Power of Attorney during their lifetime but circumstances have changed. This also deals with the situation where a donor has put in place a binding death benefit nomination which lapses after three years. The Tribunal may be in a position to provide consent to the confirmation of the nomination in circumstances where the Tribunal considers this would be consistent with the intentions of the donor who has lost capacity.[100]

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98 See, eg, Croucher and Vines, above n 38, [6.11]–[6.20].
99 Law Council of Australia, *Submission 351*.
100 Law Society of South Australia, *Submission 381*.

# Self-managed superannuation funds

7.98 The legal framework for SMSFs was established in 1999.[101] SMSFs have fewer than five members. Importantly, all fund members are also either individual trustees for the fund or directors of the corporate trustee.[102] As at June 2016, there were 577,236 SMSFs in Australia with a total of 1.1 million members.[103] There are currently over $620 billion in assets managed by SMSFs (about 29% of superannuation assets in Australia).[104]

7.99 Around 70% of SMSFs have two members and 22% are single member funds.[105] The most common structure is a super fund held by a couple.[106] While some SMSFs are established and managed by very wealthy investors, 45% of SMSFs have total balances of less than $500,000.[107] Evidence suggests that some SMSFs are used as part of a family business structure, typically with the business premises owned by the SMSF and leased to the family business.[108]

7.100 The Financial Planning Association noted that

> the people who establish and manage their own SMSF are highly engaged with their financial affairs and decision making. They are not forced to establish an SMSF, rather they choose to. And in doing so take on the responsibility and obligations of the SMSF. The regulatory requirements of establishing and managing an SMSF can be complex, so many trustees seek professional financial advice.[109]

7.101 In 2009, the Australian Government established a review into the 'governance, efficiency, structure and operation of Australia's superannuation system', known as the Super System Review Panel (the Panel).[110] The thorough examination of the SMSF sector by the Panel provides context for the recommendations that follow. The ALRC has focused on discrete targeted recommendations that seek to address the issue of reducing elder abuse, particularly among those older people who may have impaired decision-making ability. Recognising the work already undertaken by the Panel, the ALRC does not make broader recommendations affecting the legal and regulatory regime for SMSFs.

## Emerging risk of elder abuse

7.102 The ALRC received a small number of submissions raising concerns regarding financial abuse of older people involving SMSFs.[111] Submitters also noted that the rate of non-compliance identified by auditors was low at around 2% of funds.[112]

7.103 The low prevalence of elder abuse in relation to SMSFs may reflect the current demographics of those with SMSFs. Only 8.8% of SMSFs have members aged over 75

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101 *Superannuation Legislation Amendment Act (No. 3) 1999* (Cth). SMSF were previously known as excluded funds.

102 The only exception is single member funds with individual trustees where there must be two trustees one of whom is the member. See *Superannuation Industry (Supervision) Act 1993* (Cth) s 17A.

103 Australian Taxation Office, *Annual SMSF Population Analysis Tables* (2016).

104 Australian Prudential Regulation Authority (APRA), *Statistics: Quarterly Superannuation Performance June 2016* (2016).

105 Australian Taxation Office, above n 103.

106 Ibid.

107 Ibid.

108 Julie Castillo, 'The SMSFs Trustee-Members' (2012) 40(3) *Australian Business Law Review* 177, 178.

109 Financial Planning Association of Australia (FPA), Submission 295.

110 Super System Review Panel, *Super System Review Final Report* (2010).

111 Office of the Public Guardian (Qld), *Submission 173*; Financial Services Institute of Australasia, *Submission 137*.

112 Dixon Advisory, *Submission 342*.

years[113]—who may be more at risk of elder abuse given increasing rates disability and cognitive impairment. However, 55% of SMSF members are aged between 55 and 74 years of age.[114] This suggests that, in the coming decades, a greater number of older and potentially more vulnerable individuals will have an SMSF.

7.104 The risk of vulnerability to financial abuse in relation to an SMSF arises in part because the regulatory framework for SMSFs was designed on the premise of self protection. This model for SMSFs supported reduced government regulation:

> As members of self managed superannuation funds will be able to protect their own interests these funds will be subject to a less onerous prudential regime under the *SIS Act*.[115]

7.105 The different regulatory framework for SMSFs and the larger industry and retail funds regulated by APRA was explained in the following terms:

> APRA considers they have a responsibility for ensuring trustees [of those larger superannuation funds for which APRA is the responsible regulator] have properly formulated their investment strategies as set out in trustee documentation and that this can be demonstrated through practical implementation.... The Tax Office's approach is, however, consistent with past Tax Office practice and the Government's original policy intent. This intent specified that whilst SMSFs are a key vehicle in the accumulation of retirement savings, they do not require onerous prudential supervision as members should be able to protect their own interests.[116]

7.106 The emphasis on responsibility and self protection in the regulation of SMSFs was reiterated by the Panel which identified the following policy principles underpinning regulation in this sector:

> Principle 1—Ultimate responsibility
>
> Principle 2—Freedom from intervention
>
> Principle 3—… but not complete absence of intervention.[117]

7.107 A regulatory framework that relies on self protection may be problematic, however, as a larger number of SMSFs come under the control of older people who may require increasing decision-making support.

## What happens when a trustee suffers a 'legal disability'?

### *Enduring attorney to take over SMSF*

7.108 In the event that a trustee/director suffers a 'legal disability'[118] (the term used in the *SIS Act* for a lack of decision-making ability), the SMSF will become non-compliant for the purposes of superannuation law six months after legal disability unless: the principal's interest in the fund can be paid out; the fund is able to be wound up, a tribunal appoints a financial administrator who can step in as trustee/director; or the management of the SMSF is transferred to an APRA licensed trustee. If the fund becomes non-compliant for the purposes of superannuation law there may be a range of administrative and tax penalties that apply and the fund may be wound up.

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113 Australian Taxation Office, above n 103.

114 Ibid.

115 Explanatory Memorandum, *Superannuation Legislation Amendment Act (No. 3) 1999* (Cth).

116 Australian National Audit Office, *The Australian Taxation Office's Approach to Regulating and Registering Self Managed Superannuation Funds* (Report No 52 of 2006–2007, 2007).

117 Super System Review Panel, above n 110, 219.

118 *Superannuation Industry (Supervision) Act 1993* (Cth) s 17A.

7.109 The only exception is where the trustees/directors have appointed an enduring attorney, as the *SIS Act permits* an attorney to become a trustee or director of the corporate trustee for the purposes of the fund's compliance with superannuation law. Accordingly, in order to manage the situation where a trustee/director suffers a 'legal disability', it is essential that all trustees/directors have an enduring power of attorney.[119]

7.110 Importantly, the law only *permits* an enduring attorney to become a trustee/director. The law does not *require* the attorney to become the trustee nor does superannuation law override the particular terms of the trust deed and/or constitution of the corporate trustee.[120] The trust deed and constitution of the corporate trustee must allow for the appointment of the attorney as trustee and the processes set down in the document must be followed.

7.111 With respect to the situation where a person has a legal disability and their enduring attorney seeks to become the trustee or director of the corporate trustee, the ALRC notes that, aside from sophisticated investors and their professional advisers, there appears to be a general lack of awareness of the complexity that surrounds the process of appointing the enduring attorney as a director/trustee of an SMSF.

7.112 The process for an enduring attorney to take control of the SMSF on the principal's loss of capacity is not straightforward, particularly when compared to dealing with bank accounts. In those latter cases, the attorney must simply present the enduring power of attorney document in order to complete transactions from the bank account.

### *Process of appointing enduring attorney as an individual trustee*

7.113 A particular complication arises with respect to SMSFs with individual trustees, as there must be a minimum of two trustees and there are particular rules of general trust law that inhibit the ability of the remaining trustee continuing to act where one trustee has a legal disability. Unless the trust deed specifically provides to the contrary, individual trustees must act jointly; and the trustee with a legal disability continues to be a trustee until removed.[121] Accordingly, where one trustee suffers a legal disability the other trustee (or trustees) cannot make any decisions on behalf of (and in the absence of) the person who has suffered a legal disability.[122]

7.114 Therefore the key issue is how the trustee who has a legal disability may be removed and the enduring attorney be appointed. This is determined by the trust deed. Some of the most common methods included in trust deeds are for the power to be assigned to the outgoing trustee, the member(s) of the fund or, in older deeds, the 'employer sponsor' of the fund.[123] Unless carefully drafted, the trust deed may give power for the removal and appointment to the remaining trustee or members of the SMSF, rather than the enduring attorney for the individual who has suffered a legal disability. Particular legislative provisions applying to trusts generally may also be

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119 As set out in ch 5, given the complexity of managing a SMSFs, the ALRC is recommending that the enduring power of attorney must explicitly include a power to deal with superannuation.

120 Australian Tax Office, *Self-Managed Superannuation Funds Ruling,* SMSFR 2010/2, 21 April 2010 2.

121 *Muir v Inland Revenue Commissioners* [1966] 1 WLR 1269, 1283. For an excellent summary of the law in this area as it relates to SMSFs *see:* Bryce Figot, *Complete Guide to SMSFs: Planning for Loss of Capacity and Death* (CCH Australia, 2016).

122 *In the Estate of William Just deceased (No 1)* (1973) 7 SASR 508 and *Beath v Kousal* [2010] VSC 24.

123 Figot, above n 121, 49–52.

invoked giving the last surviving trustee the power to nominate a replacement for the trustee who has lost capacity.[124]

7.115 Thus a person (John) may appoint his daughter (Maria) as his enduring attorney and in that document specifically give Maria power to manage John's superannuation. Notwithstanding this, if John suffers a legal disability that invokes the enduring power of attorney, Maria will not automatically become the trustee of the SMSF. The terms of the trust deed must be followed. The terms of the SMSF trust deed may give that power to the other individual trustee, John's brother Joshua. Thus Joshua has the power to appoint the successor trustee and he may use this to appoint someone other than the principal's daughter and enduring attorney. If Joshua did this, the SMSF will ultimately become non-compliant for the purpose of superannuation law, but the immediate concern—from an elder abuse perspective—is that John's investment in the SMSF will be under the control of someone other than the person he wished to take control of his finances in the event that he suffered a legal disability. This increases the risk that those funds will not be managed in a manner that upholds John's wishes.

7.116 This type of scenario was reflected in the submission from the Financial Planning Association of Australia:

> The most common SMSF dispute when an individual member has died or lost capacity, involves the spouse of a second marriage trying to disinherit children from the first marriage, particularly where the spouse of the second marriage is a trustee and has discretion of the fund.[125]

7.117 The other complication with an individual trustee is that John's name will be on all the legal documents for all the real property and other assets of the SMSF. If Maria is successful in becoming the trustee, all the documentation will need to be changed from John's to Maria's name. Chartered Accountants Australia and New Zealand explained some of the practical challenges of effecting a change in trustee:

> [the process] can be expensive, time consuming and deeply frustrating. Depending on the assets held by an SMSF the following fees may apply for changing the ownership of fund assets:
>
> - State or Territory filing fees for changing land titles.
> - Fees, chargers or penalties imposed by financial institutions such as, banks, stock brokers and share registries.
> - Amending lease documents.
>
> In addition the administrative process and documentary proofs require to change the owner of a trust asset … will vary greatly from one entity to another.[126]

### *Process of appointing enduring attorney as a director of the corporate trustee*

7.118 Where the SMSF has a corporate trustee, the process of appointing the enduring attorney as a director is somewhat easier. There is no need to change the trustee of the SMSF, but rather there is a need to change a director of the trustee. Standard off-the-shelf corporate constitutions typically (but not in every case) have provisions that provide for automatic vacation of the position of director on the loss of capacity or legal disability. Members holding a majority of shares at a general meeting of

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124 Where the terms of the trust deed are silent or the provisions cannot be invoked (because the outgoing trustee has lost capacity and therefore can't elect a replacement trustee) See, eg, *Trustee Act 1925* (NSW), s 6; *Trusts Act 1973* (Qld) s 12 and *Trustee Act 1958* (Vic) s 41.

125 Financial Planning Association of Australia (FPA), *Submission 295*.

126 Chartered Accountants Australia and New Zealand, *Submission 368*.

shareholders are required to appoint a new director. The enduring attorney may have the authority over the shares held by the director who has suffered a legal disability to vote those shares to appoint themselves a director.[127]

7.119 Using the same example as in paragraph [7.115], but assuming a corporate trustee, John may appoint his daughter Maria as his enduring attorney and in that document specifically give Maria power to manage John's superannuation. John and Joshua are both directors of the SMSF's corporate trustee and each hold one share in the corporate trustee. Thus if John suffered a legal disability, Maria would require the votes of Joshua in a general meeting of shareholders to be appointed as a director (as both Maria and Joshua would control 50% and not a majority of shares). If Joshua did not vote for Maria to become a director, she would not become a director of the trustee. If this were to occur, the SMSF will again ultimately become non-compliant for the purpose of superannuation law, but the immediate concern—from an elder abuse perspective—is that John's investment in the SMSF will be under the control of someone other than the person he wished to take control of his finances in the event that he suffered a legal disability.

### ***Consequences of a trustee suffering a legal disability***

7.120 There are two important points from the previous discussion. First, the legal documentation for the SMSF must be drafted in a way that reflects the succession plans of the members on suffering a legal disability. Many of the documents used to establish an SMSF do not properly provide for succession events where a trustee suffers a legal disability.[128] The adequacy and currency of SMSF trust deeds is currently not scrutinised at all, either by the ATO, or the approved auditor.

7.121 Secondly, careful consideration is needed as to who is likely to have effective control of the SMSF in circumstances where a trustee suffers a legal disability. This is because the person who has control has a significant influence over whether the person's wishes for the management of their SMSF are carried out in the event of suffering a legal disability.

## Replaceable rules

**Recommendation 7–2** The *Superannuation Industry (Supervision) Act 1993* (Cth) should be amended to include 'replaceable rules' for self-managed superannuation funds which provide a mechanism for an enduring attorney to become a trustee/director where this was provided for in the enduring document and notwithstanding the terms of the trust deed and constitution of the corporate trustee or the actions of the other trustees/directors.

7.122 To address some of the challenges of effecting a desired succession in the event of a legal disability, in the Discussion Paper the ALRC asked whether the *SIS Act* should be amended to set out the steps that are to be taken when a trustee or director of the corporate trustee has suffered a legal disability.[129] The ALRC considered that these legislative parameters could provide a safety net in the event that the trustee has not

127 *Corporations Act 2001* (Cth) s 141.
128 Grant Abbott, *Guide to Self Managed Super Funds* (CCH, 3rd ed, 2006) 87.
129 Australian Law Reform Commission, *Elder Abuse*, Discussion Paper No 83 (2016) question 7–1.

already put in place an effective succession plan. This recommendation responds to that question.

7.123 Recommendation 7–2 would provide a mechanism for ensuring that a person's enduring attorney is able to step in as a trustee/director where this was provided for in the enduring document. It would overcome deficiencies in the trust deed and company constitution that would otherwise prevent the attorney taking that role. It would also override the ability of the remaining trustee(s)/directors to thwart the appointment of the enduring attorney as trustee/director.

7.124 Under the *Corporations Act 2001* (Cth) a company may choose how its internal governance structures are derived.[130] They can be: a constitution; replaceable rules; or a combination of both. A company's constitution is a contract between: the company and each member; the company and each director; the company and the company secretary, and a member and each other member.

7.125 Replaceable rules are set out in s 141 of the *Corporations Act* and can be 'replaced' by the provisions of a company's constitution. These 42 rules govern a range of matters relating to how the company:

- appoints and removes its directors;
- passes directors resolutions;
- conducts directors meetings;
- organises members meetings;
- remunerates directors;
- transfers shares; and
- pays dividends.

7.126 Where it is agreed that the replaceable rules will apply in full or in part with respect to a company, the replaceable rules operate contractually in the same way as a constitution. That is, a breach of the replaceable rules gives rise to an action for breach of contract whereby shareholders may seek a court order requiring compliance with any replaceable rules. A breach of the replaceable rules cannot lead to a prosecution for breach of the *Corporations Act*.

7.127 By drafting Recommendation 7–2 as a 'replaceable rule', individual autonomy and choice are retained, as individuals have the ability to 'replace' the rule and rely on the primacy of their trust deed/corporate constitution, particularly where those have been drafted as part of complex estate planning arrangements.

7.128 The 'replaceable rule' would be subject to the ordinary consent requirements for becoming a director and trustee. That is, the enduring attorney would have to consent to becoming a director/trustee and thus the appointment would not be immediate on the activation of the enduring power of attorney.

7.129 The replaceable rule would apply on the successful application for the fund to become a registered SMSF with the ATO, unless expressly overruled by the provisions of the trust deed and corporate constitution. Appropriate transitional arrangements would need to be in place to enable SMSF trustees and members to consider whether

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130 For a good overview of proprietary companies: see Dr Pamela Hanrahan, 'The Law of Close Corporations Australia' *International Academy of Comparative Law World Congress in Vienna 2014*.

the replaceable rule should apply and, if not, amend their documentation accordingly. The legislation would need to allow, with appropriate safeguards, for SMSF members to alter the fund documentation in the event that all members agree that a change to the applicability of the replaceable rule is required.

7.130 The recommendation would overcome concerns that significant numbers of SMSF are created with off-the-shelf documentation that has not been crafted to meet the estate planning and succession objectives of their members. It would also overcome problems created by the misperception that the law 'requires' rather than 'permits' an attorney under an enduring power to become a trustee/director. Ultimately, this would address the risk of elder financial abuse where a person other than the attorney, (being the chosen person to manage the older person's finances on loss of decision-making ability) is able to control the funds in the SMSF.

## Balancing prescription with protection

7.131 Recommendation 7–2 strikes a balance between being overly prescriptive in legislation and (limiting the fetter on SMSF trustees) while also offering protection for SMSF members who may not appreciate the complexities of planning for loss of decision-making ability in the context of their SMSF.

7.132 The idea expressed in the Discussion Paper, that the *SIS Act* should be amended to set out in legislation the steps that are to be taken when a trustee or director of the corporate trustee suffers a legal disability, received mixed views in submissions.

7.133 The GRC Institute supported the proposition that succession events be set out in legislation:

> We agree that there should be certain arrangements for loss of capacity. Many modern trust deeds that set up these arrangements do have these provisions, but a modification to the *SIS Act* incorporating additional clauses in these deeds would be appropriate.[131]

7.134 Similarly, FINSIA supported the proposition and suggested that '[t]his is particularly important for unadvised persons with SMSFs that are using off-the-shelf products'.[132]

7.135 CPA Australia also offered qualified support noting that there was 'scope to prescribe certain arrangements for the management of self-managed superannuation funds in the event that a trustee loses capacity'.[133]

7.136 The need for flexibility was emphasised by the Law Council of Australia:

> The Law Council considers that 'hard wiring' a particular course of action may be counterproductive and give rise to inappropriate results. For example, a member may have a legal personal representative but there may be reasons why having that person appointed as a trustee or trustee director in place of the member would be inappropriate in the particular circumstances. Equally, the compulsory transfer of a member's interests might give rise to adverse tax results or might unduly disadvantage the remaining member/s of the self-managed superannuation fund.[134]

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131 GRC Institute, *Submission 358*.
132 FINSIA, *Submission 339*.
133 CPA Australia, *Submission 338*.
134 Law Council, *Submission 351*.

7.137 Similarly, the SMSFA and Financial Planning Association of Australia emphasised the importance of member education rather than prescribing certain succession events in legislation.[135]

7.138 The ALRC agrees that education and awareness raising are important, but suggests that the complexity in this area may militate against their effectiveness as the only solution. As set out above, the law regarding SMSFs is highly complex and the legal arrangements for succession on suffering a 'legal disability' requires careful procedural steps be taken. While many individuals with SMSFs are highly educated and sophisticated investors, and many retain specialist advisers, there are over 1.1 million individuals who are members of an SMSF, suggesting a breadth of financial expertise. Many SMSFs have relatively small balances, suggesting not all SMSFs members would be availing themselves of specialist advice. Accordingly, the ALRC considers that this recommendation strikes the right balance, providing a mechanism to overcome deficiencies in documentation and understanding, while providing freedom to develop sophisticated estate planning strategies.

7.139 The ALRC agrees that a 'one size fits all' approach to succession events in the event of a legal disability is inappropriate and undesirable, given the diversity of SMSFs in Australia. As a result, the recommendation is drafted as a 'replaceable rule' that provides a simple mechanism for an enduring attorney to step in as trustee/director while retaining the ability of SMSF members to chose alternative courses of action if this would not be a suitable outcome.

7.140 Another reason for drafting the recommendation as a 'replaceable rule' is that, while SMSFs are most likely to be funds held by a couple or single member funds, they can be funds with up to five members, who may not be related. In the latter circumstance, the ALRC envisages that the replaceable rule is less likely to be appropriate with members unlikely to accept a situation where, irrespective of the trust deed and corporate constitution, a member's enduring attorney can step in if a member suffers a legal disability. In such circumstances, it may be that the nature of the contractual and fiduciary relationships are carefully calibrated in the SMSF documentation and the replaceable rule would upset these arrangements. Alternatively, an individual may not wish their enduring attorney to step into that role of director/trustee and wishes to replace the rule and require that their interest in the fund be paid out or transferred to an APRA-regulated fund on loss of decision-making ability.[136]

# Planning for a 'legal disability'

**Recommendation 7–3** The relevant operating standards for self-managed superannuation funds in cl 4.09 of the *Superannuation Industry (Supervision) Regulations 1994* (Cth), should be amended to add an additional standard that would require the trustee to consider the suitability of the investment plan where an individual trustee or director of the corporate trustee becomes 'under a legal disability'.

135 SMSF Association, *Submission 382*; Financial Planning Association of Australia (FPA), *Submission 295*.

136 For the reasons set out above this may not be possible where there are individual trustees.

7.141 Trustees of SMSFs must ensure that the fund complies with prescribed operating standards.[137] The relevant operating standards are set out in cl 4.09(2) of the *SIS Regulations*:

> The trustee of the entity must formulate, review regularly and give effect to an investment strategy that has regard to the whole of the circumstances of the entity including, but not limited to, the following:
>
> (a) the risk involved in making, holding and realising, and the likely return from, the entity's investments, having regard to its objectives and expected cash flow requirements;
>
> (b) the composition of the entity's investments as a whole, including the extent to which they are diverse or involve exposure of the entity to risks from inadequate diversification;
>
> (c) the liquidity of the entity's investments, having regard to its expected cash flow requirements;
>
> (d) the ability of the entity to discharge its existing and prospective liabilities;
>
> (e) whether the trustees of the fund should hold a contract of insurance that provides insurance cover for one or more members of the fund.[138]

7.142 Recommendation 7–3 recognises that planning for a legal disability, as a central protective strategy against elder abuse, needs to look beyond the legal structures for succession and consider the investments in the SMSF, and how they may be best managed in the event of a trustee suffering a legal disability.

7.143 This recommendation was suggested by the SMSFA:

> Our proposed amendment is similar to the recent addition of SIS regulation 4.09(2)(e) that requires trustees to consider whether their fund should hold insurance. This has had great success in putting insurance to the front of every trustees mind and will have the same effect with estate and succession planning. Furthermore, it then becomes a legal requirement that trustees consider estate planning and then this becomes part of the audit standards that SMSF auditors must see evidence of when auditing the SMSF financials each year.[139]

7.144 A similar reform was suggested by Dixon Advisory:

> the annual reporting requirements to the Auditor or ATO could contain a declaration stating that the trustee has considered succession planning for each of the Trustees. The annual declaration could include considerations like: the benefits of corporate trustees, the importance of appointing an appropriate enduring power of attorney and executor as well as educating the trustee appropriately on their preferences.[140]

7.145 A key part of this proposed operating standard is requiring trustees to consider whether the asset mix of the SMSF is consistent with proposed succession plans. That is, are the assets fungible on a trustee suffering a legal disability or will the assets require long term management by the trustee's enduring attorney. This brings 'front of mind' important questions as to the suitability of the chosen enduring attorney to manage the SMSF. Dixon Advisory noted that

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137 *Superannuation Industry (Supervision) Act 1993* (Cth) ss 31(1) and 34. Failure to comply can lead to the imposition of civil penalties or a criminal conviction: ss 34(2), 166.

138 A number of these obligations were introduced in July 2013 as part of the Government's *Stronger Super Package* and were designed to improve the financial health of SMSFs, recognising the absence of prudential controls over SMSFs.

139 SMSF Association, *Submission 382*.

140 Dixon Advisory, *Submission 342*.

> SMSFs often have tailored strategic approaches and unique investments that require individualised management strategies. Noting our increasing life and retirement phase expectancy, it is entirely appropriate for SMSF trustees to hold investments that have a long term focus. SMSF trustees may also hold business and residential property, unlisted assets and other sophisticated investments which can, at times, be less liquid. A prescribed event, such as rolling a member out of the SMSF within a set period of time, may cause significant losses for the members and beneficiaries in these situations.[141]

7.146 As the requirement to review the SMSF's investment strategy for consistency with succession planning for loss of legal capacity would be an operating standard of SMSFs, trustees would be required to demonstrate to the SMSF's auditors that they have considered their investment strategy in light of the potential for loss of capacity by a director/trustee. Regular reviews through the audit process should encourage consideration of appropriate succession planning and focus on the need to keep the plan up to date. This addresses a key risk for older people in relation to SMSFs: that many members do not understand, or have not considered, how lack of planning for the possibility of a legal disability may make them susceptible to elder abuse.

7.147 Recommendation 7–3 only requires trustees to 'consider a plan', not to have a plan, or a plan of a particular type. This retains ultimate control with the trustee—consistent with the regulatory approach for SMSFs. It is also consistent with the view expressed by submitters that a 'one size fits all' approach to succession on loss of capacity would be problematic given the diversity and complexity of SMSFs in terms of both their assets and structure.[142]

7.148 The ALRC recognises that the regulation was amended in 2012 to require trustees to consider whether their fund should hold insurance. There is no data on the uptake of insurance following the implementation of this requirement. Recommendation 7–3 would add only a limited regulatory burden as it would not require SMSFs to do any more than consider planning for the loss of capacity by trustees/directors as part of the fund's investment strategy.

# Australian Taxation Office notification

**Recommendation 7–4** Section 104A of the *Superannuation Industry (Supervision) Act 1993* (Cth) and the accompanying Australian Taxation Office Trustee Declaration form should be amended to require an individual to notify the Australian Taxation Office when they become a trustee (or director of a company which acts as trustee) of a self-managed superannuation fund as a consequence of being an attorney under an enduring document.

7.149 Since 1 July 2007, s 104A of the *SIS Act* has required that a person, on becoming a trustee, or director of a company which acts as trustee, of an SMSF sign an ATO approved form—the ATO Trustee Declaration.

7.150 According to the ATO, the purpose of the declaration is primarily educative—reinforcing the roles and responsibilities that are attached to running an SMSF.[143] The

141 Ibid.

142 Ibid.

143 Australian Taxation Office, *Trustee Declaration (NAT 71089).*

declaration contains information on trustee duties, the sole purpose test, investment restrictions and rules regarding the administration of the SMSF.[144]

7.151 The declaration must be signed within 21 days of being appointed as a trustee, or as a director of the company acting as trustee. There is no requirement to send the declaration to the ATO. The obligation is simply to retain the declaration for as long as the person is a trustee or director of the company and in any event for at least 10 years.[145] The ATO may request to see a copy of the declaration at any time. It is an offence not to sign the declaration within the 21 day period, to fail to provide a signed declaration to the ATO when required, and to fail to retain the signed declaration.[146]

7.152 Existing trustees/directors also have an obligation to ensure that a new trustee/director signs the ATO Trustee Declaration within the 21 day period. Further, the other trustees/directors must ensure that the signed declaration is retained for the required period and provided to the ATO as and when requested.[147]

7.153 Currently, there is little additional oversight when an individual becomes a trustee/director of an SMSF pursuant to an enduring power of attorney. SMSFs are subject to less regulation on the principle of individual choice and control. This is attenuated when a person loses capacity and the central feature of SMSFs is broken—that the beneficiary and manager of the funds are the same person. ATO notification would bring to the regulator's attention SMSFs that may need greater scrutiny and attention.

7.154 The requirement to lodge the form would signal to the new trustee/director the seriousness of the obligations and would highlight the role of the ATO as the regulator of SMSFs. The obligation to lodge the form also ensures the form is read and signed. This cannot be guaranteed with the current arrangement where there is no specific obligation to lodge the form with the ATO.

7.155 Recommendation 7–4 builds on suggestions from both Dixon Advisory and the SMSFA in relation to trustee notifications and annual returns. The SMSFA suggested:

> a simple amendment to the SMSF Annual Return that is lodged with the ATO allowing SMSFs to alert the ATO when an EPOA has been used in the administration of the fund. This can be established by a 'tick box' and will provide a flag to the ATO of which funds may now be at higher risk for elder abuse.[148]

7.156 Dixon Advisory highlighted the important educative value of the ATO Trustee Declaration. The ALRC considers that the declaration is the appropriate vehicle for informing the ATO that an enduring attorney has taken over as trustee/director. While the SMSFA's suggestion of including this information in the annual return has merit, it is less immediate than the ATO Trustee Declaration, which would need to be lodged within 21 days. In addition, the annual return is a broader requirement to lodge the accounts of the fund whereas the ATO Trustee Declaration requires specific focus on the individual responsibilities that apply to trustees/directors.

7.157 The ALRC notes that SMSFs are subject to audit requirements and that these requirements were strengthened in 2013. In this context, it could be argued that, as SMSFs are already subject to regular audits, there may be marginal benefit in making the ATO aware that an individual has been appointed because a member has suffered a

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144 Ibid.
145 *Superannuation Industry (Supervision) Act 1993* (Cth) s 104A.
146 Ibid.
147 Ibid.
148 SMSF Association, *Submission 382*.

legal disability so that they can apply greater scrutiny. Nevertheless, the broader regulatory framework for SMSFs needs to be taken into account. There is less oversight and regulation of SMSFs because those running the funds are the beneficiaries. Where that is not the case, because a member has suffered a legal disability, it is appropriate to provide a legislative basis for the ATO to apply greater scrutiny.

# Other areas for reform of self-managed superannuation funds

7.158 In the Discussion Paper, the ALRC considered a number of other issues that are not subject to final recommendation, such as whether the *SIS Act* should be amended to:

- require that all SMSFs have a corporate trustee;
- impose additional compliance obligations on trustees and directors when they are not a member of the fund; and
- give the SCT jurisdiction to resolve disputes involving SMSFs.[149]

7.159 The ALRC also considered whether there should be restrictions as to who may provide advice on, and prepare documentation for, the establishment of SMSFs. This section considers these issues and the responses from stakeholders.

## Corporate trustee or individual trustees

7.160 The majority of SMSFs have individual trustees rather than a corporate trustee.[150] The Super System Review Panel (the Panel) noted that it is 'widely accepted by professionals and the ATO that a corporate trustee is superior'.[151] Benefits included:

- perpetual succession—the corporate entity cannot die, so it enables better control in the event of member death or incapacity;
- greater administrative efficiency;
- greater flexibility to pay benefits as lump sums or pensions;
- greater estate planning flexibility; and
- reduced risk of deliberate or accidental intermingling of fund and personal assets, in breach of the covenant in s 52(2)(d) of the *SIS Act*.[152]

7.161 The Panel concluded that it

> is attracted to the potential benefits provided by the corporate trustee structure and is concerned about the large proportion of new SMSFs choosing not to use a corporate trustee. However, consistent with principle 2 regarding freedom from intervention, the Panel believes that the solution here is a better standard of advice, an aim which is addressed by other recommendations.[153]

7.162 Given the greater protection afforded by a corporate trustee, the ALRC sought feedback from submitters as to whether there should be a change in the law requiring a corporate trustee for new SMSFs.

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149 Australian Law Reform Commission, *Elder Abuse*, Discussion Paper No 83 (2016) question 7–1.
150 Australian Taxation Office, above n 103.
151 Super System Review Panel, above n 110, 223–224.
152 Ibid.
153 Ibid 224.

7.163 There was broad recognition of the benefits of a corporate trustee when compared to an individual trustee.[154] However, there was significantly less support for mandating a corporate trustee for all SMSFs. For example:

> The Law Council does not think that the *Superannuation Industry (Supervision) Act 1993* (Cth) (*SIS Act*) should be amended to require that all new self-managed superannuation funds have a corporate trustee. While the Law Council considers that there are strong reasons in favour of such a structure … it does not believe that requiring this to be adopted would of itself reduce the risk of elder abuse occurring.[155]

7.164 Other reasons put forward against mandating a corporate trustee were that it would reduce individual choice, impose additional costs and increasing complexity.[156] The ALRC considers that a corporate trustee, when compared to individual trustees, has numerous benefits (as outlined above) and may contribute to reducing the risks of elder abuse in the context of a loss of legal capacity. However, mandating a corporate trustee would be a significant reform that would have consequences for the entire SMSF sector that cannot be justified solely on the basis of addressing elder abuse.

## Improving documentation

7.165 The Panel noted some of the challenges created by the regulatory regime for SMSFs, which requires a fund to be established by private documentation rather than by legislation.[157] Establishment by private documentation results in most individuals being reliant on professional advice for the establishment of their SMSF.[158] Advisers are typically accountants and financial advisers. Lawyers may or may not be engaged to draft the trust deed and the constitution for the corporate trustee.

7.166 Accordingly, in the Discussion Paper, the ALRC sought views about how documentation for SMSFs could be improved to protect against poor documentation facilitating abuse in the context of a loss of decision-making ability. The ALRC also asked about how to improve the quality of professional advice provided in respect of SMSFs.

7.167 Stakeholders acknowledged that the documentation for SMSFs could be improved and that there was an overreliance on generic documents. However, there was a view that this was driven by consumer choice rather than a lack of qualifications or expertise by those preparing documentation.[159]

7.168 In relation to the advice provided on the establishment of an SMSF, many stakeholders pointed to the recent tightening of the rules around who could provide advice on the establishment of SMSFs.[160] Since 30 June 2016, accountants must now have an Australian Financial Services Licence in order to provide advice regarding the establishment of an SMSF. The SMSFA submitted that this has further strengthened the quality of advice surrounding the establishment of SMSFs for a large population of advisers.[161]

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154 For example: SMSF Association, *Submission 382*; Chartered Accountants Australia and New Zealand, *Submission 368*; FINSIA, *Submission 339*. Stakeholders also suggest that the corporate trustee should be a sole purpose company to protect against co-mingling of funds.

155 Law Council, *Submission 351*. Citations omitted.

156 See, eg, GRC Institute, *Submission 358*; Dixon Advisory, *Submission 342*; CPA Australia, *Submission 338*.

157 Super System Review Panel, above n 110, 270.

158 Castillo, above n 108, 181.

159 Dixon Advisory, *Submission 342*.

160 Ibid.

161 SMSF Association, *Submission 382*.

7.169 As a result, many suggested no legal reforms were required. For example:

> Dixon Advisory submits that the vast majority of times, a wide array of professionals are engaged to ensure that the establishment of and running of SMSFs is consistent [with the law]. Further, there are also compulsory documents for the establishment of SMSFs which need professional supervision or approval before they are valid.[162]

7.170 The ALRC is of the view that establishing and running an SMSF is a complex undertaking and that not all those who embark on that course are necessarily sophisticated investors. The ALRC considers that Recommendation 7–2 above, to provide a 'replaceable rule' in relation to succession on loss of capacity will overcome many issues with documentation that is poorly prepared or not suitably tailored to the specific requirement of the SMSF members.

## Access to the Superannuation Complaints Tribunal

7.171 If a member of an APRA-regulated superannuation fund has a dispute with the fund, the member may access the SCT for dispute resolution.[163] There is no access to the SCT for members of SMSFs. Essentially, this is because members are also trustees and therefore a dispute between a member and the fund is circular. In its Issues Paper, the Panel raised the potential of extending the jurisdiction the SCT to SMSFs,[164] but decided against it. This conclusion was based on a view that a large proportion of disputes would relate to individuals who were dissatisfied with an SMSF trustee decision regarding a BDBNs and otherwise in relation to complex family law disputes.[165]

7.172 In the Discussion Paper, the ALRC suggested that, where an SMSF member is no longer a trustee because they have a legal disability, there may be a role for the SCT in providing a low-cost forum for disputes. There may also be a role for the SCT in providing advice to trustees on request, and in approving conflict of interest transactions similar to the role played by state civil and administrative tribunals in relation to enduring powers of attorney.[166] The ALRC sought stakeholder views on this issue.

7.173 There was some support in submissions for the SCT having such a role.[167] However, the majority of submissions were opposed to expanding the jurisdiction of the SCT to SMSFs. For example, the Law Council of Australia considered

> it would not be appropriate to involve the SCT in disputes that are ultimately disputes between family members or associates and are private in nature. … The SCT is set up to support individuals in dispute with third party trustees who may be disadvantaged by other legal avenues. It is not equipped to deal with related party disputes.[168]

7.174 Additionally, it was noted that the SCT is self-funded, and expanding its jurisdiction would increase costs which would have to be borne by all superannuation fund members. It was also suggested that SMSF disputes were unlikely to be limited to superannuation matters and that the tribunal would therefore only be able to address

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162 Dixon Advisory, *Submission 342*.

163 *Superannuation (Resolution of Complaints) Act 1993* (Cth).

164 Super System Review Panel, '*Phase Three: Structure (Including SMSFs) Issues Paper*' (14 December 2014).

165 Super System Review Panel, above n 110.

166 Rec 5–2.

167 FINSIA, *Submission 339*; Public Trustee of Queensland, *Submission 249*.

168 Law Council, *Submission 351*. See also Chartered Accountants Australia and New Zealand, *Submission 368*.

part of a dispute relating to superannuation law and not matters relating to corporations law or family law.[169]

7.175 Stakeholders also drew attention to the fact that the SCT is currently under review. On 5 May 2016, the Australian Government established an independent expert panel to review the financial system's external dispute resolution and complaints framework. On 6 December 2016, the expert panel released an interim report making a number of findings with respect to the SCT—including that it was subject to significant delay in resolving complaints, that it is under resourced and its governance arrangements need to be reformed with a need for greater transparency in operations.[170] The interim view of the expert panel is that the SCT should be replaced with an ombudsman type model.

7.176 The ALRC considers that SMSF members do need access to a low-cost forum for dispute resolution. In light of the expert panel's ongoing review of dispute resolution in the financial sector, further consideration of the SMSF sector's need for dispute resolution forums should be considered as part of the work of the expert panel.

### *Additional obligations on trustees and directors*

7.177 There are now a range of statutory obligations imposed on attorneys under state and territory powers of attorney legislation, in addition to general law fiduciary duties owed to the principal. However, when an attorney becomes a director or trustee in relation to an SMSF, they do so in their personal capacity and not in their capacity as attorney.[171] Accordingly, they would not be bound by the additional statutory obligations that have been imposed on attorneys under state and territory powers of attorney legislation.[172] In that role they are bound by the general law of fiduciary duties of trustees or the *Corporations Act,* and not the state and territory powers of attorney legislation. The ALRC sought submissions on whether these protections are sufficient.

7.178 Submissions were generally of the view that the existing obligations and protections were sufficient.[173] For example, Dixon Advisory submitted that

> the wide array of responsibilities imposed on trustees are sufficient to ensure a regulated approach in managing the affairs of the member. The imposition of further requirements would not only create confusion and overlap in the operation of the laws, but may potentially create obligations that infringe and restrict the way that a large majority of bona fide trustees operate.[174]

7.179 The Association of Financial Advisers (AFA) noted that an enduring attorney stepping into replace a trustee who has lost decision-making ability is not the only time that the law permits trustees/directors not to be members of an SMSF. When an SMSF has a corporate trustee it can have additional non-member directors and the AFA

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169 Law Council, *Submission 351*; Dixon Advisory, *Submission 342*.

170 Professor Ian Ramsay, Julie Abraham and Alan Kirkland, *Interim Report—Review of the Financial System External Dispute Resolution and Complaints Framework* (2016).

171 See [7.110]

172 Therese Catanzariti, '"There in Spirit" Powers of Attorney in the SME Context' (13 Wentworth Chambers, 2012). The relevant duties include: *Corporations Act 2001* (Cth) ss 180–182

173 This was not a universal view of submitters. FINSIA agreed that additional compliance obligations should be applied to assist with the correct use of SMSF funds. See FINSIA, *Submission 339*.

174 Dixon Advisory, *Submission 342*. Similar views were expressed in the following submissions*:* GRC Institute, *Submission 358*; Financial Planning Association of Australia (FPA), *Submission 295*; Financial Services Council, *Submission 78*.

submitted that differentiating between directors that are members and those that are non-members in terms of legal duties and obligations would be problematic.[175]

7.180 The Law Council of Australia also suggested that

> [t]o impose additional compliance obligations in respect of what is already a highly regulated and onerous role may simply make it difficult for older persons to find an individual willing to take on the role (noting that this must be unpaid).[176]

7.181 Accordingly, the ALRC considers that at this time no additional obligations on trustees and directors should be imposed where they are appointed as a result of being an enduring power of attorney for a trustee/director that has suffered a legal disability.

175 Association of Financial Advisers (AFA), *Submission 346*.
176 Law Council, *Submission 351*.