

New ATO ID released: impact for SMSF succession planning

The ATO has released interpretative decision ATO ID 2011/77. It is highly relevant for SMSF succession planning.

The scenario considered

ATO ID 2011/77 considers when a stepchild ceases to be a child of a stepparent. Naturally, this is a vital question because:

- under the *Superannuation Industry (Supervision) Act 1993* (Cth) a child is a dependant and
- under the *Superannuation Industry (Supervision) Regulations 1994* (Cth) a dependant may receive superannuation death benefits.

Accordingly, what this ATO ID is answering is when a stepparent's superannuation death benefits may be paid to a stepchild.

More specifically, it answers whether a stepparent's superannuation death benefits may be paid to a stepchild if the stepparent divorced from the stepchild's biological parent before death.

The answer

The ATO states that a stepchild ceases to be a dependant upon divorce. In other words, if:

- person A was married to person B
- person A and person B have child C (ie, child C is the biological child of both person A and person B)
- person A and person B divorce
- person A and person D marry
- person A and person D divorce
- person D dies

then child C is ineligible to receive person D's superannuation death benefits.

However, the position might be different — that is child C might still be able to receive person D's superannuation death benefits — if any of the following are true:

- person D and child C were in an interdependency relationship
- person D legally adopted child C

- child C was financially dependent upon person D.

The implications

Firstly, remember that an ATO ID is not the law. However, assuming that the view in ATO ID 2011/77 is correct (which DBA Lawyers believes it to be), then it has several key implications.

The most obvious implication is that superannuation fund trustees typically may not pay out person D's superannuation death benefits to child C.

This implication gives rise to a subsequent, less obvious, implication. Namely, non-biological children of superannuation fund members typically cease being beneficiaries of the fund upon divorce.

It surprises many to learn that this is often very positive news for superannuation funds. Remember that the beneficiaries of a superannuation fund are much broader than the members. Further, beneficiaries have various rights, such:

- compelling proper administration of the fund by the trustee
- having the trustees act in good faith and
- inspecting trust documents, including the governing rules (eg, the trust deed) and trust accounts.

Accordingly, children of a member's former spouse can't use such rights to make a nuisance of themselves (or use them as leverage in a family law property settlement negotiation).

The bigger question

However, there is a bigger question that is not expressly addressed by ATO ID 2011/77.

The question is best illustrated with the following common example.

Hugh is married to Julie. Julie is Hugh's second spouse. Hugh has a child from his previous relationship (Hugh Junior).

When Hugh dies he wants Julie to be provided for by way of a non-commutable pension from his SMSF. When Julie dies, Hugh then wants Hugh Junior to receive the capital from the pension.

Hugh wants to know whether this is possible. In other words, when Hugh dies, is Hugh Junior still Julie's

child and thus able to receive Julie's death benefits upon her death?

ATO ID 2011/77 does not expressly answer this question. However, it quotes with approval certain case law that suggests that the answer is no. In other words, ATO ID 2011/77 suggests that upon Hugh's death, Hugh Junior ceases to be Julie's dependant. This is consistent with the ATO's view expressed in the June 2011 NTLG Superannuation Technical Sub-group:

the stepchild/step-parent relationship is severed when the marriage of the parent ceases, that is, upon the death of the natural parent or upon the divorce of the natural parent from the step-parent.

Therefore, any superannuation death benefits that Julie might have upon death can not be paid directly to Hugh Junior. Instead, those benefits would have to be paid to Julie's estate. Hopefully then:

- Julie's will would provide that any superannuation death benefits received by the estate would be paid to Hugh Junior and
- Julie's estate would not be challenged (eg, by a testator's family maintenance claim).

Further steps

If Hugh wanted to pursue this structure, he might consider further steps to 'lock in' this structure, such as:

- implementing a mutual wills agreement (to provide recourse in case Julie does change her will)
- Julie legally adopting Hugh Junior (naturally however this would be fairly extreme and quite uncommon) and
- Considering whether there is any other scope to say that Hugh Junior is a dependant for reasons of financial dependency or interdependency.

However, none of these further steps guarantee certainty. If Hugh really values certainty, he might even consider a more extreme option such as withdrawing benefits from superannuation during his life and placing them in a family discretionary trust with an independent trustee where Julie is an 'income beneficiary' and Hugh Junior is a 'capital beneficiary'.

More information

These issues and many more are discussed in DBA Lawyers' publication *The Complete Guide to SMSFs and Planning for Loss of Capacity and Death*.

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