



Managing Incapacity Risk in SMSFs

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Introduction

This paper is to accompany the power point presentation slides entitled “Managing Incapacity Risk in SMSFs” to be presented as a Webinar with Television Education Network.

This paper will consider the following:

1. Estate planning issues to consider;
2. The definition of a “self-managed superannuation fund”: section 17A of the *Superannuation Industry (Supervision) Act 1993* (Cth) (“**the SIS Act**”) and trustee requirements;
3. Who determines whether a member/trustee is incapacitated;
4. Evaluating the trustee member and shareholder structure of the fund;
5. Determining who controls the fund on incapacity of each member;
6. Use of powers of attorney for each member;
7. Addressing incapacity in the fund deed and corporate trustee constitution;
8. Determining who has voting rights attaching to share impacted by incapacity;
9. Power to appoint or remove fund trustee; and
10. Addressing deadlock in voting situations.

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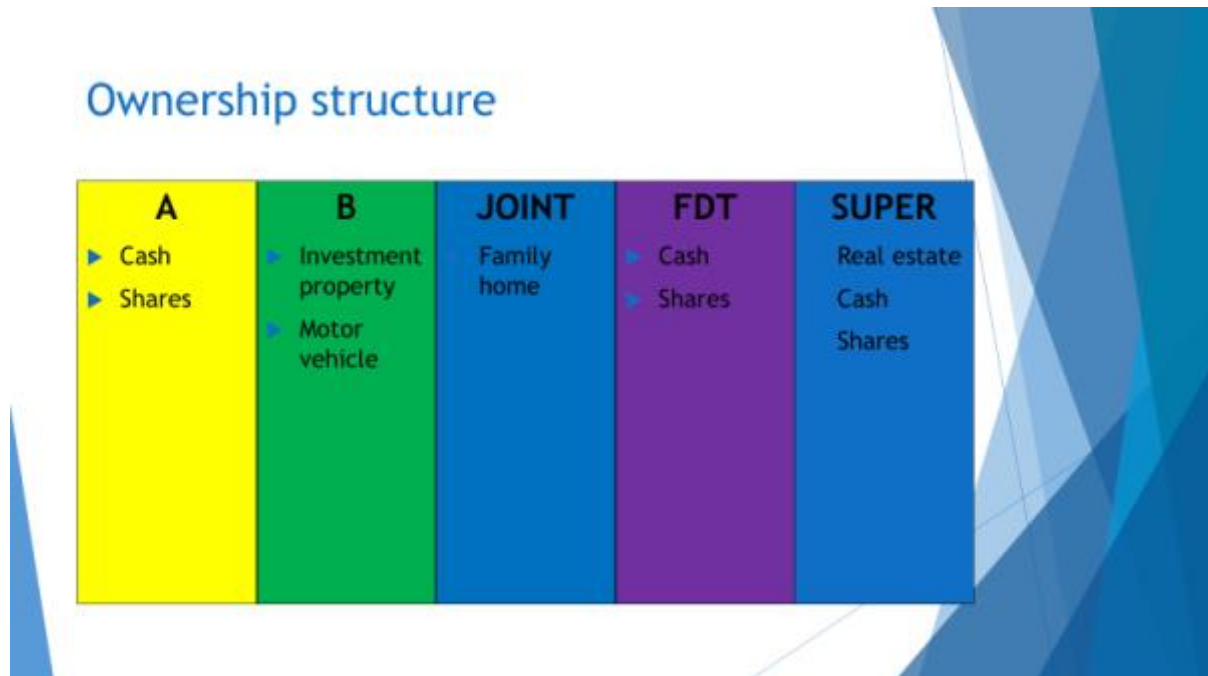
STRUCTURING & TAX
SMSFs & TRUSTS
ASSET PROTECTION
ESTATE & SUCCESSION PLANNING
DISPUTE RESOLUTION & LITIGATION
DECEASED ESTATE ADMINISTRATION & PROBATE

LIABILITY LIMITED BY A SCHEME APPROVED UNDER PROFESSIONAL STANDARDS LEGISLATION

Estate planning and the “four worlds”

1. By way of introduction, an estate planner should generally be aware of four worlds that a client (or their beneficiaries) may face, such as:
 - (a) Estate challenge risk;
 - (b) Taxation and duty;
 - (c) Bankruptcy and asset protection concerns; and
 - (d) Family law risk.
2. Whilst the above four “worlds” are relevant to any estate plan, it is important to minimise risk of abuse by ensuring the right controllers are present. This includes control during one’s lifetime, in the event of loss of capacity and on death. This is because controllers (in the form of trustees, shareholders or directors of companies) will essentially be able to dictate how assets are to be dealt with, administered or used for the benefit of the individual in question.
3. Essentially, prevention is far better than any cure and gone are the days where simple Wills and powers of attorney would address an individual’s estate planning. A careful review, potential restructure and implementation of control and governance mechanisms is often necessary to minimise the risk of abuse, particularly where an elderly individual is susceptible to manipulation or being outvoted by children or other “interested” third parties.

Possession is nine tenths of the law – recognise the ownership structure and know the controllers



4. In an estate planning context generally, it is extremely important that estate planners are made aware of how their clients own assets. Assets in family discretionary trusts and superannuation funds do not necessarily form part of one’s estate. Ascertaining the ownership structure from an elderly individual is crucial to ensure that they are aware as to

how their assets are owned, and how they are controlled and who can control them during their lifetime, on loss of capacity and on death.

5. Below is a summary of how assets are dealt with during one's lifetime, on loss of capacity and on death:

Structure	Lifetime (with capacity)	Incapacity	Death
Personally held	Individual	Financial attorney or administrator	Executor or administrator subject to Will or intestacy laws
Jointly held	Individuals jointly	Financial attorneys or administrators (jointly with the other joint proprietor)	Surviving joint proprietor
Company	Individual shareholders and directors, subject to constitution Shareholders' agreement	Shareholders: financial attorneys/administrators, constitution Directors: constitution Shareholders' agreement	Shareholders: executor or administrator subject to Will or intestacy laws Directors: subject to surviving directors, constitution Shareholders' agreement
Trusts	Trustees/appointors: trust deed, corporate trustee constitution	Trustees/appointors: Deed, corporate trustee constitution, subject to financial powers of attorney Shareholders/directors of trustee company: financial attorneys, subject to corporate trustee constitution	Trustees/appointors: deed and succession provisions Shareholders of trustee company: executor or administrator subject to Will or intestacy laws and directors subject to corporate trustee constitution
Superannuation (in particular SMSFs)	Individual (member level and trustee level): trust deed, corporate trustee constitution	Financial attorney or administrator: trust deed, corporate trustee constitution Note SMSFR 2010/2	Trustee: surviving trustee and/or LPR: executor or administrator No BDBN: trustee discretion (surviving trustee and/or LPR): trust deed, corporate trustee constitution BDBN: direction by member

6. This paper will focus on control of SMSFs, but the other structures above are worth noting.

The definition of a “self-managed superannuation fund”: section 17A of the SIS Act; evaluating the structure of the SMSF

Structure and governance of a self-managed superannuation fund

7. An Australian self-managed superannuation fund (“**SMSF**”) has the following officeholders:
 - (a) Trustees, which manage the fund on a day to day basis including the making of investment decisions. The trustees can be individuals or a company.
 - (b) Members, who are able to contribute funds (or have funds contributed on their behalf) to form part of their account balance.
 - (c) The Australian Taxation Office, which is the watchdog overlooking the administration of SMSFs to ensure that the fund in question is compliant with the legislative framework, ie superannuation and tax law.
8. As the law currently stands, SMSFs must have a minimum of one member and a maximum of four members.¹ On 30 June 2020, the Federal Government announced a revised start date for a change to a new maximum of six members to be effective from future Royal Assent.²
9. As the law currently stands (with 1-4 member SMSFs), there are specific requirements for members to be represented at the trustee level:
 - (a) In the case of a single member SMSF:³
 - (i) If the trustees are individuals, the member together with one other individual (either a relative or person other than the member’s employer) must be represented at the trustee level; and
 - (ii) If the trustee is a company, the member must either be appointed as the sole director or a director together with one other director (who is either a relative or a person other than the member’s employer).
 - (b) In the case of an SMSF with 2-4 members:⁴
 - (i) If the trustees are individuals, all members are to be represented at the trustee level; and
 - (ii) If the trustee is a company, all members are to be appointed as directors of the company.
10. Above all, the trust deed contains the governing rules of the fund which determine the rights and obligations of the trustee, members and other parties who deal with the fund. The trust deed should be the primary reference in relation to the operation and governance of an SMSF.
11. The trustee has the obligation to carry out the terms of the trust which are contained in the trust deed. Notwithstanding legislation which is permissive (and provides what you can and

¹ See s 17A of the *Superannuation Industry (Supervision) Act 1993* (Cth) (“**the SIS Act**”).

² <https://ministers.treasury.gov.au/ministers/michael-sukkar-2019/media-releases/revised-start-dates-technical-superannuation-and>

³ See subsection 17A(2) of the SIS Act.

⁴ See subsection 17(1) of the SIS Act.

cannot do – see below), the trust deed is seen to be prescriptive and may contain other procedural requirements which need to be followed in relation to the administration of the fund.

12. There are three main laws that govern SMSFs, in particular:
 - (a) The *Superannuation Industry (Supervision) Act 1993* (Cth) (“**the SIS Act**”) which spells out the compliance issues relating to superannuation funds including borrowing restrictions, prohibited investments and the sole purpose test;
 - (b) The *Income Tax Assessment Act 1997* (Cth) (“**the ITAA97**”) which spells out the taxation implications of superannuation funds (and benefits received from superannuation funds) and thresholds relating to members’ contributions to the fund; and
 - (c) The *Corporations Act 2001* (Cth) which governs the appointment and removal of directors, directors’ duties (in the case where a company has been appointed to act as trustee as an SMSF) and sets out the disclosure and licensing requirements of financial products and financial service providers.

13. Control lies with the trustee (either individuals or a company with the fund’s members represented at director level). The decision-making provisions are contained in the trust deed and/or company constitution (if a corporate trustee is used). These documents should contain provisions relating to:
 - (a) Processes relating to meetings of members, trustees (as well as shareholders/directors of the corporate trustee);
 - (b) Investment powers;
 - (c) The process to appoint and remove a trustee; and
 - (d) Dispute resolution mechanisms in the event of a dispute between the parties, eg portability or other rights of the members.

Lifetime decision-making

14. During the lifetime of members, the following decisions may often need to be made within the fund:
 - (a) Investment decisions;
 - (b) Accessing benefits (eg as a lump sum, or commencing a pension) if and when a condition of release has been met;⁵ and
 - (c) The preparation of binding death benefit nominations as part of their estate and succession planning.

15. Each trust deed is different and contains mechanisms which deal with such decisions within the fund. For instance, some deeds require trustees to obtain the consent of members when

⁵ See eg, retirement, attaining the age of 65 years, permanent incapacity, terminal illness outlined in Schedule 1 of the SIS Regs.

exercising certain powers, and some deeds/constitutions require a majority vote of trustees/directors to make a decision. Some deeds go further to require the trustees to accept and/or acknowledge receipt of a binding death benefit nomination. The decision-makers at the trustee and/or shareholder/director level in the corporate trustee may therefore significantly impact (or curtail) critical decisions being made within the fund.

Recommendation for a corporate trustee

16. In structuring an SMSF, it is generally recommend that a sole purpose company be used to act as trustee. The reason for this is that it would be administratively easier for all the parties involved on the death or loss of capacity of a member of the SMSF, such as the surviving members and legal personal representative of the deceased or incapacitated member.
17. Under trust law, the assets of a SMSF (which is a form of trust) are held by its trustee(s). Due to the operation of section 17A of the SIS Act, where a member dies or loses capacity, steps will need to be taken to ensure that the member is effectively removed from control of the SMSF and that the member's legal personal representative is appointed in place to control or co-control the SMSF on his or her behalf. See the section below titled "Determining who controls the SMSF on the incapacity of the member" on the succession of control of the SMSF on a member's incapacity. Given that the assets of a SMSF are to be held by its trustee(s), the title of the assets of a SMSF will need to reflect the entity or persons who will in control of the SMSF at the trustee level, on the death or incapacity of a member.
18. Where the trustees of a SMSF are individuals and a member is incapacitated, title to the assets of the SMSF will need to be changed to reflect the member's legal personal representative on title. This can be administratively troublesome and time-consuming where the SMSF holds lumpy assets such as real estate.
19. On the other hand, if the trustee of a SMSF is a corporate trustee, the trustee of the SMSF remains the same even on the incapacity of a member and will continue to hold the assets of the SMSF. All that is required to be done is to remove the member from directorship of the corporate trustee and to appoint the member's legal personal representative in his or her place.

Should children be included as members?

20. The more members (as well as controllers) there are, the higher the risk of a dispute. This is particularly the case where children are admitted as members to the fund together with their parents. In my view, extreme caution and care must be exercised when children are admitted to the same fund as their parents, with specific tailoring and drafting of the trust deed to include dispute resolution mechanisms or an exit strategy if there is a falling out between parties.
21. Some issues come to mind when including children in the SMSF with their parents:
 - (a) **Children firstly need to be included as co-trustees.** Where individual trustees are appointed, the children need to be added to the asset registers (eg real estate). However, where a corporate trustee is used, the children can be added as co-directors of the company.
 - (b) **How should decisions be made at the trustee level.** Where a "standard" company constitution is used for the corporate trustee, a significant risk is that the parents could be outvoted by a majority vote of their children if they are all in the same fund.

Consideration ought to be given to whether the constitution should be tailored to require different voting (eg a unanimous vote or a member-balance vote) when making decisions on behalf of the trustee.

- (c) **Portability issues.** Note that SMSFs are expressly excluded from the portability rights regime under Division 6.5 of the SIS Regs. For instance, if there is a dispute between members within an SMSF, they do not automatically have the ability to roll their benefits out to another fund. A tailored trust deed which enables members to transfer their benefits to another fund should be considered in the context where multiple individuals are included in the fund.
 - (d) **Family law.** In the event of relationship breakdown of a member, their superannuation is also potentially divided under the *Family Law Act 1975* (Cth). Where their superannuation is co-invested with other members within the fund in say lumpy assets, this may adversely affect the other members' interests if, for instance, an affected member's benefits have to be paid out under family law orders or an agreement.
 - (e) **Lumpy assets within the SMSF.** This is particularly the case where minimum pensions need to be paid out of the fund or the death of a member. If there is insufficient cash reserves held back within the fund, a sale of assets will need to be effected to enable minimum pension payments. Further, a member's death benefits must be paid out as soon as practicable after their death as death is a compulsory cashing requirement under superannuation law.
22. For the above reasons, it is absolutely critical that parents are made aware of the issues that come about where children are added as members of the SMSF, particularly on the death of one parent or if one or both of them were to lose decision-making capacity, when children could potentially abuse their decision-making position at the trustee level.

Who determines whether a member/trustee is incapacitated?

23. Under common law, adult individuals are presumed to have capacity to make their own decisions. This was reiterated in the case of *Goddard Elliot (a firm) v Fritsch* [2012] VSC 87, by Bell J at paragraph 545:

"The common law treats human individuals as having legal personality and thus the capacity for legal rights and obligations. The individual is taken to have legal personality because 'rights and duties involve choice' and individuals 'naturally ... enjoy the ability to choose'. For people, legal personality is thus a birthright. This foundational principle of the common law is also an international human right which, in Victoria, is protected by the Charter of Human Rights and Responsibilities Act 2006 (Vic)."

24. A member of an SMSF may lose capacity due to their age, illness, medical condition or physical accident. The question then becomes, who determines whether the individual has lost legal decision-making capacity. Usually a medical practitioner's report is key in determining whether the individual has legal decision-making capacity.
25. If indeed an individual has lost capacity, there are consequences that need to be thought through, including:
- (a) Is the individual automatically removed as an (individual) trustee?

- (b) Is the individual automatically removed as a (corporate trustee) director?
 - (c) Does the individual continue on as a member of the fund?
 - (d) Who gets to make decisions including exercising the right to appoint and remove the trustee or make binding death benefit nominations?
26. The terms of the trust deed (and if relevant) the constitution of the corporate trustee are crucial in addressing these issues. The terms of the documents will usually state that the trustee or director is automatically removed on loss of capacity.
27. However, where an individual has lost capacity but the documents are silent on point:
- (a) They can be removed as a trustee (by the members under the terms of the trust deed) or director of a corporate trustee (by the shareholders under the terms of the constitution) or by a Court and steps can be taken under the terms of the documents to appoint the legal personal representative in their place; but
 - (b) They remain on as a member of the SMSF and the legal personal representative can exercise financial powers on behalf of the member under the terms of the trust deed.

Determining who controls the SMSF on the incapacity of the member

28. Recall that under section 17A of the SIS Act, a member must be represented at the trustee level of the SMSF (either as an individual trustee or a director of the corporate trustee). There are exceptions to this rule, particularly if an individual member loses capacity or dies.
29. Under paragraph 17A(3)(b) of the SIS Act, the legal personal representative of the member can act as a trustee/director of the corporate trustee during any period when:⁶
- (a) The member is under a legal disability; or
 - (b) The legal personal representative has an enduring power of attorney in respect of the member of the fund.
30. Section 10 of the SIS Act defines the “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.”*
31. Where a member loses capacity, that member’s appointed attorney under an enduring power of attorney in respect to financial members can become the trustee/director of the corporate trustee and control the fund and this is further articulated in the section of this paper entitled “Use of powers of attorney”. The preparation and use of powers of attorney as an important tool in the succession of control of SMSFs and is also vital in maintaining a fund’s compliant status in the event an individual member loses capacity.
32. Notably, an administrator appointed by a State or Territory administration tribunal in respect of an incapacitated member is able to be appointed as a trustee/director of the corporate

⁶ See paragraph 17A(3)(b) of the SIS Act.

trustee of an SMSF in place of that member under section 17A(3)(b) of the SIS Act. This was confirmed by the Commissioner in ATO Interpretative Decision 2010/139.

Use of powers of attorneys for each member

33. In light of subsection 17A(3)(b) of the SIS Act, where an individual has a self-managed superannuation fund, it is absolutely crucial that an enduring power of attorney relating to financial matters has been prepared as part of the individual's estate and succession plan. This is to ensure that the fund retains complying status as a self-managed superannuation fund under section 17A, should the individual member lose capacity.
34. The Australian Taxation Office has released SMSF Ruling SMSFR 2010/2 which provides the Commissioner's opinion on how subparagraph 17A(3)(b)(ii) of the SIS Act applies to SMSFs where the legal personal representative has an enduring power of attorney over the member of the fund.
35. In particular, in the Commissioner's view:
 - (a) A person who holds an enduring power of attorney qualifies as their "legal personal representative" for the purposes of section 17A;
 - (b) The power of attorney must be current, accord with the state/territory laws relating to enduring powers of attorney;
 - (c) The attorney must be appointed as a trustee under the governing rules of the fund or a director of the corporate trustee under its constitution, and the member must be removed as a trustee/director in accordance with the trust deed/constitution (unless the attorney is appointed as an alternate director of the corporate trustee); and
 - (d) If the attorney is appointed as a trustee/director, they perform their duties as trustee/director pursuant to their appointment of that position rather than attorney/agent of the member.⁷
36. Therefore, the choice of financial attorneys in these circumstances is crucial as they will ultimately hold a very powerful position in relation to the control and administration of the fund. The member appointing an attorney must be comfortable that the attorney will have their best interests at heart as the attorney would be able to unilaterally make certain decisions in the event the member loses capacity. This is particularly the case in an elder law setting on loss of capacity where the attorney would need to make decisions on their behalf.
37. SMSFR 2010/2 also provides several examples of the application of substitute decision-makers in the SMSF context, including:
 - (a) Where an attorney is already a member (and trustee/director of the corporate trustee) of the fund;⁸

⁷ The Commissioner notes in paragraph 11 of SMSFR 2010/2 that consequently, any proscriptions contained in state/territory legislation against conferring trustee duties and powers via a power of attorney or common law restrictions on attorneys undertaking directors duties are not relevant to the application of paragraph 17A(3)(b)(ii) of the SIS Act.

⁸ See Example 2 at paragraph 22 of SMSFR 2010/2.

- (b) Where an attorney is not a member of the fund;⁹ and
 - (c) Multiple attorneys being appointed;¹⁰
 - (d) Appointments of alternate directors at the corporate trustee level.¹¹
38. Where substitute decision-makers are to be appointed, it is critical that SMSFR 2010/2 be read together with the governing rules of the SMSF and the enduring power of attorney.
39. Consideration ought to be given to whether the power of attorney document's terms are expressly permissive, prescriptive, silent, or whether they prohibit an attorney acting (in particular, for more bespoke arrangements).
40. Where an attorney as substitute decision-maker is appointed as a replacement trustee/director of the corporate trustee, it would be prudent that this be documented in a trustee minute to confirm the compliance with section 17A of the SIS Act, in addition to change of trustee or director documentation.

Powers of attorney and binding death benefit nominations

41. A question that has often been asked is whether a financial attorney is able to make or revoke a binding death benefit nomination.
42. We have finally been given some judicial guidance on this point in the recent decision of *Re Narumon Pty Ltd*.¹² In that case, Mr Giles (the deceased member) prepared a binding death benefit nomination on 5 June 2013 which nominated 47.5% of his death benefits to be paid to his wife Mrs Giles, 47.5% to his son and 5% to his sister Mrs Keenan (notably, Mrs Keenan as Mr Giles' sister was not a SIS dependant). The nomination stated that it would lapse 3 years after the date of signing (ie on 5 June 2016). In March 2016, Mrs Giles and Mrs Keenan signed an "extension of binding death benefit nomination" document to renew the 2013 binding nomination. They also signed a new binding death benefit nomination, nominating Mrs Giles and the son to each receive 50% of the death benefits (after realising that Mrs Keenan was not a SIS dependant and was not eligible to receive superannuation death benefits directly from the fund).
43. The Court held that the new binding death benefit nomination was void on the basis that the attorneys were in a position of conflict as the recipients of benefits under the binding nomination and further, the power of attorney did not expressly authorise the conflict. However, the Court held that the renewal document was valid, with the remaining 5% (which Mrs Keenan was nominated to receive), to be paid at the trustee's discretion. The Court also noted:
- (a) That the SMSF trust deed did not adopt the requirements in regulation 6.17A of the SIS Regs, even though the trust deed required binding nominations to comply with "Superannuation Law" (which included the SIS Regs);

⁹ See Example 1 at paragraphs 20-21 of SMSFR 2010/2.

¹⁰ See Example 4 at paragraphs 25-28 of SMSFR 2010/2.

¹¹ See Example 5 at paragraphs 29-31 of SMSFR 2010/2.

¹² [2018] QSC 185.

- (b) That although the nomination of Mrs Keenan was not valid (as she was not a SIS dependant – as defined below), this did not invalidate the rest of the nomination in respect of Mrs Giles and the son’s entitlements (as they were SIS dependants);
 - (c) Although the trust deed was silent as to whether an attorney could make a binding nomination on behalf of a member, attorneys could make a binding nomination in accordance with the Queensland laws relating to powers of attorney;
 - (d) An attorney making a binding nomination in favour of themselves will be void as the attorney needs to avoid conflicts of interest unless the power of attorney expressly authorises a conflict; and
 - (e) An attorney confirming/extending/renewing/making a binding nomination on the same terms as their last nomination appears to be authorised.
44. Where an enduring power of attorney is proposing to make a binding death benefit nomination on behalf of a member, a review of the trust deed and the enduring power of attorney documentation is crucial. In particular:
- (a) What special conditions or limitations are included in the power of attorney?
 - (b) Does the power of attorney authorise a conflict, expressly allowing an attorney to make a binding death benefit nomination in favour of themselves?
 - (c) What does the trust deed say? Does the trust deed preclude attorneys from making binding death benefit nominations?

Trustee appointment following the death of a member

45. Another issue that has been uncertain is the transition of control of the a SMSF from the attorney to the executor, when an incapacitated member subsequently passes away, and where his or her appointments of attorney and executors are different individuals.
46. This issue was explored in the recent case of *Dawson v Dawson* [2019] NSWSC 826 (“**Dawson**”). In that case:
- (a) Peter Dawson and his spouse Estelle Dawson (being the first defendant) were the individual trustees of a SMSF which was established in 2005.
 - (b) In 2012, Peter and Estelle separated.
 - (c) In 2013, Peter appointed his son from a previous relationship, Tony Dawson (being the plaintiff), as his attorney under an enduring power of attorney.
 - (d) In 2014, Tony was appointed as a trustee of the fund in Peter’s place after Peter lost capacity.
 - (e) Peter passed away on 24 November 2015.
47. George Holland (being the second defendant) was appointed as executor of Peter’s estate and probate of his Will was granted to him. By deed of confirmation dated 6 April 2018, the defendants purported to confirm and ratify a prior change of trustee on 24 November 2015 being the date of Peter’s death, that Tony was removed as a trustee of the fund and George

was appointed in his place. The basis of the deed of confirmation according to the defendants was that on Peter's death, Tony's power of attorney ceased. Consequently, Tony should automatically be removed as trustee of the Fund and George should be appointed in his place. Tony disputed the appointment of George as a trustee and commenced proceedings.

48. Henry J of the Supreme Court of New South Wales noted the following in his judgement:
- (a) Where an attorney is appointed as a trustee of a fund in place of an incapacitated member, they are appointed in their personal capacity, not as an attorney or agent for the incapacitated member. Tony was therefore held to have been appointed as trustee of the fund in his personal capacity and was acting in his personal capacity as trustee pursuant to his appointment as trustee rather than as attorney or agent for Peter.
- This means that a trustee of an SMSF once appointed (whether they are also the attorney for a member) may be personally liable for any breaches of trust and may be subject to civil and criminal penalties for breaches of duties.
- (b) Where an attorney is appointed as a trustee of an SMSF in place of an incapacitated member, their appointment does not automatically cease upon the member's subsequent death and their cessation will depend on the terms of the trust deed for the SMSF. Given that Tony was appointed in his personal capacity as the trustee of the Fund and that the terms of the fund did not provide for the cessation of Tony's appointment on Peter's death and did not place limits on his appointment, he will continue to be the trustee of the fund until he ceases to hold office as provided for under the fund's trust deed.
 - (c) The appointment of George as a trustee of the fund was invalid. For George's appointment to be valid, the appointment had to be made in accordance with the terms of the fund's trust deed, namely by the consent of the trustees of the fund who were Tony and Estelle at that time. Given that Tony did not consent to George's appointment, his appointment was accordingly invalid.
49. Notably, an issue in *Dawson* was whether the fund was a one-member or two-member fund following Peter's death. The reason for this is that the determination of this question would determine who should have been a trustee of the fund in order to comply with the SIS Act. Henry J held that if the fund remained a two-member fund following Peter's death (and before the payment of his death benefits) it was necessary to appoint George (as Peter's legal personal representative) as the trustee within 6 months after Peter's death for the fund to be a complying SMSF under subsection 17A(3) of the SIS Act.
50. Henry J was of the view that the fund had remained a two-member fund and had not yet transitioned into a one-member fund.¹³ However, George had not been appointed as a trustee on Peter's death due to the invalidity of George's appointment as a trustee.
51. The case of *Dawson* emphasises the importance of the choice of financial attorneys as they will ultimately hold a very powerful position in relation to the control and administration of the fund, potentially extending beyond the death of the member and the cessation of the power of attorney.

¹³ See reasons outlined in paragraphs 112 to 122 of the judgment.

52. In order to minimise the risk of disputes that arose in *Dawson*:
- (a) A corporate trustee should be used to act as the trustee of the SMSF, instead of individual trustees. The executor of the deceased member would be able exercise the deceased member's shareholder rights in the corporate trustee to appoint themselves as a director, as well as remove the attorney where the attorney is still a director of the corporate trustee; and
 - (b) Appointments of attorney(s) under a member's enduring power of attorney in respect of financial matters should be mirrored with the executor appointment under the terms of the member's Will. This would ensure a smooth transition from the attorney role on the incapacity of the member, to the executor role on the subsequent death of the member, and minimise the risk of disputes.

Addressing incapacity in the SMSF deed and corporate trustee constitution

53. Aside from the provisions of the SIS Act and the terms of the enduring powers of attorney in relation to financial matters, the constituent documents of the SMSF will have to be reviewed in relation to the event of incapacity. The constituent documents of the SMSF generally include the governing rules of the SMSF (namely the SMSF trust deed and any other amending deeds) and the constitution of the corporate trustee (if any).
54. If a member loses capacity, subject to the trust deed or the company constitution (as the context requires):
- (f) Where the SMSF has an individual trustee(s), that member will be automatically removed as a trustee; and
 - (g) Where the SMSF has a corporate trustee, that member will be automatically removed as a director.
55. It will then be up to the legal personal representative to either appoint themselves as an individual trustee or corporate trustee director in the place of the deceased member, provided they are able to do so on behalf of the member (eg as a shareholder of the corporate trustee, or as a member individually, if individual trustees are in place).
56. The case of *Ioppolo v Conti*¹⁴ highlights that in the context of death, a member's legal personal representative is not automatically appointed as a replacement trustee or corporate trustee director but instead, the trust deed is key in determining who can become the trustee on death. The case also highlights that possession is nine-tenths of the law, with the surviving controller (or person appointed as legal personal representative who ultimately assumes control of the fund at the trustee level) is what really matters as they in fact hold the "purse strings".
57. Although this case specifically addresses matters in the context of the death of a member, the same issue arises in the context of loss of capacity; that is, a member's legal personal representative is not automatically appointed in the trustee role and the specific procedures outlined in the trust deed or company constitution (as the context requires) need to be followed in relation to the appointment of the legal personal representative as a replacement trustee or a director of the corporate trustee.

¹⁴ [2015] WASCA 45 (10 March 2015).

58. A legal personal representative is therefore able (and is not compelled) to take steps to appoint themselves as successor controller of the SMSF under paragraph 17A(3)(b) of the SIS Act.
59. It is accordingly crucial that the constituent documents for the SMSF contemplate the event of incapacity to ensure that the terms therein provide an appropriate mechanism for the legal personal representative of the incapacitated member to step into the shoes of the member and administer the SMSF for the benefit of that member, in particular:
- (a) Where the SMSF has individual trustees, to appoint themselves as a trustee of the SMSF;
 - (b) The trust deed authorises the attorney to do or carry out any act a member is lawfully authorised to under the governing rules of the SMSF or superannuation law as a member of the SMSF, such as making or renewing a binding death benefit nomination (as discussed above); and
 - (c) Where the SMSF has a corporate trustee, to enable the legal personal representative of the incapacitated member to be appointed to the board of directors of the company, perhaps without the need to go through a shareholders' resolution under the *Corporations Act 2001* (Cth).
60. While it is equally important that enduring powers of attorney relating to financial matters are prepared, and that section 17A(3)(b) of the SIS Act can be relied upon to allow a legal personal representative to be appointed as a trustee or director of the corporate trustee, the process of succession of control of the SMSF to the legal personal representative may lead to delays or disputes where the constituent documents for the SMSF do not clearly outline the procedures and processes for the succession of control to occur.
61. Notably, a clear distinction should be drawn between:
- (a) The legal personal representative stepping into the shoes of the incapacitated member, as a member of the SMSF; and
 - (b) The legal personal representative being appointed in place of the incapacitated member as a director of the corporate trustee of the SMSF.
62. The former should be dealt with in the governing rules of the SMSF (ie the trust deed) and the latter should be dealt with in the company constitution of the corporate trustee. Confusing the two may result in any mechanism for the succession of control (whether as a member of the fund or as a corporate trustee director) to be ineffective.
63. For example, provisions included in the SMSF trust deed pertaining to the removal of the incapacitated member as a director of the corporate trustee and the appointment of the legal personal representative in that member's place would be ineffective as those matters are only dealt with in the constitution of the corporate trustee.

Determining who has voting rights attaching to shares in corporate trustee impacted by incapacity

64. Generally, where a SMSF has a corporate trustee, the members of the fund would also be directors as well as shareholders of the corporate trustee.

65. A shareholder in a company has rights (rights to dividends, capital on a winding up and voting), with such rights defined under the terms of the company's constitution. Such voting rights include the right to vote to appoint a director of the company.
66. When devising an estate plan for an individual, the choice of one's legal personal representative (financial attorneys and executors) is absolutely critical given that they would be the successor controllers of the fund on the death or incapacity of an individual, to comply with section 17A of the SIS Act. In particular, if a member is also a shareholder in the corporate trustee, the legal personal representative would simply exercise shareholder rights to appoint themselves as director of the company.

Power to appoint or remove fund trustee.

67. The mechanisms dealing with the appointment and removal of trustees of SMSFs under the terms of the trust deed are crucial in determining who holds this power.
68. Whilst each trust deed prescribes different procedures to be followed, the power to appoint or remove trustees generally rests with the members of the fund. Therefore, whilst the fund's members are alive and have capacity, they should be able to remove the trustee under the terms of the trust deed. The trust deed in question will prescribe the number of members required to remove the trustee from office, eg a unanimous decision, a simple majority decision or 75% majority.
69. In the circumstances where a member has lost capacity, the individual's duly appointed attorney may be able to step into the shoes of the member on their incapacity to act in removing the trustee from office. Whether they can do this is largely dependent on any specific provisions of the trust deed disallowing this. However, where the trust deed is silent, I am of the opinion that the attorney is able to exercise the power to remove on behalf of the member.
70. A member's choice of attorney is therefore critical, given that in addition to controlling the fund at the trustee level, they may be able to remove the trustee from office by exercising powers of the member, under the terms of the trust deed.

Addressing deadlock in voting situations

71. To minimise the risk of voting deadlocks and conflicts, it is important to firstly review the existing constituent documents of the SMSF in light of the appointed trustees/directors, members, attorneys and executors of the individual and to consider the worst case scenario as to what could go wrong in the administration of the SMSF or payment of benefits.
72. An appropriate plan should then be implemented, particularly for funds with multiple members (such as children). For instance the trust deed and corporate trustee constitution (if applicable) could:
- (a) Include member balance voting rules (rather than voting rights linked to mere membership in the fund) for the members, trustees/directors. This would minimise the risk of a parent (with a significant sum in superannuation) being outvoted by their two children who may only each a substantially smaller amount in the fund.
 - (b) Include dispute resolution mechanisms to be resorted to in the event there are disputes between members, trustees or both – eg amicable resolution, mediation and then arbitration before considering Court proceedings.

- (c) Expressly include portability rules which enable an individual member to request the trustee to transfer their benefits to another superannuation fund, noting that the compulsory portability rules in Division 6.5 of the SIS Regs do not apply to SMSFs.¹⁵
 - (d) Do away with any unnecessarily complex “procedures” which need to be followed in relation to the adoption of a binding death benefit nomination. For instance, there is no need for the binding nomination to be accepted by or given to the trustee¹⁶
 - (e) Be express about the extent of power a member’s enduring power of attorney has, eg whether the attorney can make or revoke a binding death benefit nomination (and if so, perhaps an express provision such that the attorney is only able to make a binding nomination if the enduring power of attorney expressly authorises such actions).
73. The dynamics of each family and fund is different, and the above is a list of the issues which should be considered and implemented, as appropriate.

Conclusion

74. Understanding how control of a SMSF will pass on the incapacity of a member is important in determining how one should structure a SMSF and administer the assets held therein during an individual’s lifetime, to cater to the event that one or more members lose capacity. Carefully thought through mechanisms for SMSFs should be implemented in the estate planning process to ensure an individual is protected as much as possible and the risk of the maladministration of the SMSF to the detriment of the incapacitated member is minimised.
75. An understanding of the controllers (and who is required to be a controller) is also critical to maintain an SMSF’s complying status with law. However, one must consider who is to become the replacement controller and substitute decision-maker on the incapacity of a member. Further, possession is nine-tenths of the law and it is important that appropriate attorneys and executors be appointed.
76. Whether a binding death benefit nomination is prepared also depends on the individual’s circumstances and estate planning objectives, and that the recent case of *Narumon* demonstrates that attorneys could be empowered under the enduring power of attorney to make or confirm a binding death benefit nomination on behalf of an incapacitated member.
77. In the absence of a binding death benefit nomination, the surviving controllers of the SMSF and are able to make a call as to how death benefits are paid out and it is important to make sure that the individual has the right controllers in place. Of course, the legal personal representatives are able to appoint themselves as controllers, but are not required to under the SIS Act, to pay out death benefits.

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¹⁵ See regulations 6.30 and 6.33 of the SIS Regs.

¹⁶ See an example of procedures in *Cantor Management Services Pty Ltd v Booth* [2017] SASCFC 122 where the trust deed required that the binding nomination be given to the trustee for it to be validly prepared.

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