

Can you use Superannuation and Life Insurance to pay Estate Debts?

IRDI Legal (December, 2017)

We have received an increasing number of enquiries relating to the use of superannuation and life insurance to satisfy debts of the estate. This question often comes from executors who are faced with an estate with limited or insufficient bank account and other accessible funds to pay for funeral expenses.

Generally speaking, Australian legislation will **not** allow superannuation or life insurance assets to be used to pay debts and liabilities of a deceased estate, even if the estate is insolvent (see section 116 of the *Bankruptcy Act 1966* (Cth)). The reasons for this and some limited exceptions are outlined below.

Superannuation funds

Part of an executor or administrator's responsibilities is to pay the liabilities of an estate from the available estate assets. While superannuation is an 'asset', it is slightly different to normal monetary or tangible assets and is not automatically considered as part of an estate. Whether it can be used to satisfy estate debts will in many cases depend on whether a beneficiary has been specifically nominated by the deceased through a 'binding death benefit nomination' (**BDBN**).

If no beneficiary has been nominated:

If no direct beneficiary has been nominated by the deceased, the superannuation fund trustee will determine how the money is to be paid. Typically the proceeds of the superannuation fund will be paid to the estate for the executor to distribute and pay outstanding debts. In this case, a creditor (such as a family member who has paid for funeral and testamentary expenses) will generally be entitled to reimbursement.

If a beneficiary has been nominated:

If the deceased has nominated a beneficiary through a BDBN:

- the superannuation fund trustee has the power to distribute any money in the fund according to those direct instructions;
- the beneficiary of the BDBN is solely entitled to the money held within it - regardless of whether the estate has any debts owing; and
- the release of superannuation funds must be carried out according to the specific terms of the BDBN or as specifically directed by the deceased prior to death.

In this case, pursuant to section 143 of the *Superannuation Act 1922* (Cth), the superannuation assets will generally not be available to the executor to pay debts and liabilities of the estate (such as funeral costs).

As each superannuation fund's rules are different, it is important to determine whether your particular fund allows for binding death benefit nominations or whether it is likely to pay to the estate in any event. For example, Government funds will in most instances pay the proceeds of a fund to the deceased's estate, while many other funds will only make a determination after consideration of factors such as the wishes of the dependants of the deceased and whether there is a binding death benefit nomination.

Life insurance policies

Sections 204 and 205 of the *Life Insurance Act 1995* (Cth) protect life policies from being applied or made available to pay the debts of a deceased estate. However, this protection does not extend to funeral and testamentary expenses which can be paid out of the policy proceeds.

If it is the policy holder's intention that their life insurance proceeds should be used to satisfy estate debts (other than funeral and testamentary expenses), they are required to either:

- 1 enter into an agreement with the life insurance provider that expressly provides for the proceeds to be applied to estate debts;
- 2 charge the money with the payment of the debt (in other words using the life insurance proceeds as collateral for the repayment of a debt); or
- 3 make an express direction in their Will that the proceeds are to be applied toward any outstanding debts of the estate.

While using a life policy to pay estate debts may have capital gains tax advantages, it should be considered in light of the particular estate circumstances and with appropriate expert advice.

How can you be protected?

The legislative protection afforded to life insurance policies and superannuation funds highlights the importance of members specifying how the proceeds of their policy or fund are to be distributed following their death. This is best achieved through the completion of:

- a binding death benefit nomination form; and
- a Will which reflects your specific personal circumstances and intentions.

How can I find out more?

IRDI Legal provides a thorough estate administration service which is tailored to your personal circumstances. Our experienced **Wills and Estates team** can assist you with all aspects of your estate planning and administration including preparing and advising on Wills and binding death benefit nominations. Please contact us to find out more.