

Article Information

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Are life insurance policies protected from a deceased person's post-death tax liabilities?

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Ms Clauson, the plaintiff acting in her capacity as administrator of the estate of Patrick John David McKeon (the deceased), sought advice as to whether she would be justified in administering the estate of the deceased as an insolvent estate.

Specifically, Ms Clauson wished to resolve legitimate doubts as to her proper administration of the estate and if she would be justified in:

(a) administering the estate on the basis that the proceeds of three insurance policies on the life of the deceased (policies issued by Abbey Life Assurance Company, TAL Life Limited and Metlife Insurance Limited the last of which was owned by PricewaterhouseCoopers Nominees (NSW) Pty Ltd under a group life plan) were not liable to be applied in payment of the debts of the deceased pursuant to s205(1)(a) of the Life Insurance Act 1995 (Cth) (Act); and

(b) retaining the proceeds of the deceased's Sunsuper superannuation policy and not applying those proceeds in payment of the debts of the deceased.

The deceased died intestate on 7 May 2014 and was survived by Ms Clauson (his de facto spouse) and four children. The deceased's estate comprised a NAB bank account (fully offset against a NAB business loan) and personal items estimated at \$23,000.00. The insurance policies totalled the amount of \$3,135,424.69 and the Sunsuper superannuation policy included a death benefit lump sum of approximately \$700,000.00.

The estate was liable for a number of unsecured liabilities, the most significant of which was the NAB business loan estimated at \$849,769.30 and tax liabilities of approximately \$1.2 million. Some of the tax liabilities were incurred prior to the deceased's death but the majority (estimated to be in the sum of \$983,384.90) were a "post-death" liability.

The Commissioner for Taxation intervened in the proceedings as an interested party. The Commissioner accepted that the proceeds of the deceased's Sunsuper superannuation policy were unavailable to the estate's creditors, it not forming part of the deceased's estate.

In regard to the insurance policies, the Commissioner submitted that s205 of the Act only provides that proceeds of a policy effected on a person's life are protected from paying debts incurred prior to the death of the person but not debts incurred after that person's death. In particular, the Commissioner submitted that funeral and testamentary expenses, post-death liabilities and legal costs incurred by the administrator are not "the person's debts". It was argued that the life insurance policies were therefore liable to be applied to those debts.

The Commissioner relied on various cases such as *In re Wertheim* [1934] VLR 321 where it was held that the phrase "his debts" was confined to debts incurred during the life of the deceased and that the proceeds of a life policy was available to satisfy those debts.

In her judgment, Chief Justice Ward considered the fact that there is a line of authority weighing in favour of the construction advanced by the Commissioner. She did not consider it open to her to depart from these authorities in circumstances where there are decisions of relatively long standing concerning legislation clearly antecedent to s205 of the Life Insurance Act 1995.

Her Honour further considered that, although there is considerable force in the view that one should not read into s205 any temporal distinction between “pre-death debts” and “post-death debts”, in view of existing authorities, the Commissioner’s construction is the one that should be adopted at least at first instance.

Her Honour held that the word “debts” in the relevant provisions was to be read as the ordinary debts of the deceased, being those incurred by the deceased in the course of his lifetime and that the life insurance policies were therefore not protected in respect of the tax liabilities as they were incurred after his death.

It is not uncommon for life insurance policies to be used as an estate planning tool, particularly to provide a financial benefit to beneficiaries including spouses and, in the case of blended families, children from previous relationships. Careful and strategic planning is required when setting up such policies as to who are the policy owner and the beneficiary. One has to question whether the administrator would not have been liable to pay the post-death debts if she had in fact been the owner of the policy or the nominated beneficiary and not the deceased debtor.