The New Super Splitting Laws

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Introduction

The *Family Law Legislation Amendment (Superannuation) Act 2001* ("the FL Superannuation Act") received Royal Assent on 28 June 2001. It is an important piece of legislation that has significant implications for a number of professional groups including family lawyers, superannuation lawyers, superannuation trustees and administrators, accountants and financial planners. It is vital that the scheme be well understood by all professionals so that proper advice can be given to clients about the complex requirements to be observed.

The complexity in the scheme arises primarily because of the complexity in the superannuation industry. If superannuation existed in the form of fully vested accumulation (sometimes referred to as defined contribution) plans only, the scheme would be relatively straightforward. The court would have the jurisdiction to make orders in respect of the subject matter, valuation would be relatively straightforward and trustees would be able to create new interests or roll the split over to another fund. However, superannuation does not exist in one form only. It is more complex than that. The new scheme has been designed to cater for all forms of superannuation and because of the universal coverage of the scheme, complex law is the result.

The scheme will commence on 28 December 2002, allowing time for the necessary changes within the superannuation industry, both software and administrative as well as familiarisation and training. The FL Superannuation Act has a default commencement provision being 18 months from the date of Royal Assent unless a proclamation is issued for the scheme to commence earlier. It was intended that once the Regulations were made, a proclamation would be issued to fix a day for commencement. However, no proclamation was issued following the making of the

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regulations, and the default commencement date therefore applies, being 28 December 2002.

Background and History

The problem of the division of superannuation has been the subject of a number of law reform reports[2], However, this is the first occasion on which this very thorny problem has been translated into an Act of Parliament. How to deal with superannuation in property settlements has bedevilled the Court since its inception in 1976. In *Crapp and Crapp*[3], the Full Court set aside the first instance decision and held that superannuation was not property within the meaning of the Family Law Act. In so deciding, Fogarty J commented about the unsatisfactory nature of the treatment of superannuation. He said at different points:

> Were it not for the presence of the superannuation fund interest the result of this case would have been highly predictable and the ambit of the discretion under sec 79 would have been fairly narrowly confined. However, the superannuation fund interest introduces into the matter a further element which is very much of the future, has real elements of uncertainty about it and is highly subjective in its evaluation. It is a matter in relation to which different Judges may arrive at differing conclusions[4].
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> ….
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> The result frequently is that the Court is forced into a position which of its very nature is incapable of producing a satisfactory result to the parties in many cases, and often resulting in a real sense of grievance in one or both of the parties[5].

The case law is replete with similar sentiments. For example, in *Harrison and Harrison*[6] the Full Court said:

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[2] Australian Law Reform Commission, Matrimonial Property, Report No 39, 1988;Joint Select Committee, Report into Certain Aspects of the Operation and Interpretation of the Family Law Act 1975, 1992, Senate Committee on Superannuation and Financial Services, Broken Work Patterns, 1995; Attorney-General's Department, Working Paper on Superannuation, 1992.

[3] (1979) FLC ¶90-615

[4] (1979) FLC ¶90-615 at 78,186

[5] (1979) FLC ¶90-615 at 78,185

[6] (1996) FLC ¶92-682

> The various attempts which trial Judges in their ingenuity have made to take superannuation entitlements into account by reference to precise mathematical calculations, although perhaps desirable from a practical point of view, nevertheless do not enable them to include such sums as property of the parties, however calculated[7]

In 1987, the Australian Law Reform Commission examined the issue and concluded that prospective superannuation benefits should be taken into account. The draft Bill produced by the Commission had a provision which gave the court the power to:

> determine, as at the relevant day, the amount that is equal to so much of the amount of the value of the notional benefit to the party under a superannuation scheme as is fairly attributable to the length of the period, or of the aggregate of the periods, during which the parties cohabited (whether married to each other or not).[8]

The draft Bill also contained provisions about how to value the superannuation interest and, through its general property power, gave the parties equal shares of all property which of course included superannuation. The work of the Commission was not implemented.

In 1992, the Joint Select Committee into Certain Aspects of the Operation and Interpretation of the Family Law Act 1975 made a general recommendation that:

> to the extent possible within constitutional power, the Family Law Act be amended to include superannuation entitlements as property.[9]

A working group was established within the Attorney-General's Department to address the recommendations made by the ALRC and the Parliamentary Joint Select Committee but its work was not completed.

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[7] (1996) FLC ¶92-68 at 83,084

[8] Australian Law Reform Commission, Matrimonial Property, report No 39, Australian Government Publishing Service, 1987, p263.

[9] Joint Select Committee on Certain Aspects of the Operation and Interpretation of the Family Law Act 1975, Commonwealth of Australia, 1992, p251.

Interlocking Legislation

The new scheme has its genesis in a position paper released in 1998.[10] The reform package contains four main pieces of legislation which interlock to enable the court to make orders to split superannuation on marriage separation. The pieces of legislation are:

- *Family Law Legislation Amendment (Superannuation) Act 2001*;
- *Family Law (Superannuation) Regulations 2001*;
- *Superannuation Industry (Supervision) Amendment Regulations 2001 (No 3)*; and
- *Family Law Legislation Amendment (Superannuation) (Consequential Provisions) Act 200l.*

There are two further elements of the legislative package yet to emerge. The first relates to amendments to the *Retirement Savings Accounts Act 1997* to ensure coverage of that type of financial product and the second relates to consequential amendments to the *Social Security Act 1991* and the *Veterans' Entitlements Act 1986* concerning super splitting in the payment phase.

The *Family Law Legislation Amendment (Superannuation) Act 2001* was introduced into the House of Representatives on 13 April 2000. On 10 May 2000, the Bill was referred to the Senate Select Committee on Superannuation and Financial Services The Senate Committee called for submissions but extended the deadline until the exposure draft of both the Family Law (Superannuation) Regulations 2001 ("the FL Regulations") and the Superannuation Industry (Supervision) Amendment Regulations 2001 (No 3) ("SIS Regulations") were released. This release occurred on 10 October 2000.

The Senate Committee issued an interim report on 28 November 2000. It reported there was almost universal support for the principles and policy objectives of the

[10] *Superannuation and Family Law: A Position Paper*, Commonwealth of Australia, May 1998.

Bill[11]. However, while there was general support for the objectives in the Bill, the Senate Committee identified four areas where it appeared that matters needed to be addressed:[12]

- Jurisdictional and other legal uncertainties about the power and operation of the Family Court;
- Perceptions about constitutional uncertainty of the Bill;
- Other legal issues; and
- Cost to the revenue and industry of implementing the Bill and associated regulations, together with the impact on trustees.

The Bill was subsequently amended to the satisfaction of the Senate Committee and after seeing the draft Regulations, the Bill received bipartisan support and was passed by Parliament on 18 June 2001.

The Essential Features of the New Scheme

Coverage of the New Super Splitting Laws

Superannuation plans covered by the definition of superannuation fund in section 10(1) of the *Superannuation Industry (Supervision) Act 1993* ("the SIS Act") in the SIS Regulations (although not necessarily regulated under the SIS regime) include superannuation provided in the private sector (which includes self managed superannuation plans), superannuation provided in the public sector, constitutionally protected plans, exempt public sector plans, judges' plans and parliamentary plans. A critical point to note is that even though a superannuation plan is not regulated under the SIS regime, the plan may still fall within the SIS definition and by virtue of that, it

[11] Senate Select Committee on Superannuation and Financial Services, *Interim Report on the Provisions of the Family Law Legislation Amendment (Superannuation) Bill 2000*, November 2000, p9.
[12] Ibid, p18.

will be covered by the new scheme.[13] The coverage is wide and it is difficult to conceive of a form of superannuation which is not covered.[14]

It will be important for practitioners to understand the following types of superannuation:

- an accumulation interest;
- a self managed superannuation interest;
- a retirement savings account;
- a small superannuation accounts interest
- a partially vested accumulation interest;
- a percentage only interest; or
- a defined benefit interest[15].

The reason for identifying the type of interest is because the interest will be treated, including its valuation, in a particular way.[16] Each type of superannuation will follow a different path ending in either the creation of a new interest in the superannuation plan, roll over or transfer or being the subject of a payment split.[17]

An accumulation interest is one which is valued by taking the contributions (both employer and employee) together with interest earned, less any charges or taxes. It is the simplest form of superannuation and in the case of unitised funds, the value can be obtained on a daily basis.

Self managed superannuation funds (SMSFs) must meet five conditions[18]:

- the fund must have fewer than 5 members;

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[13] For a full discussion of the coverage provided by the SIS Act definition see Australian Superannuation Law and Practice, CCH, ¶2-165.

[14] The Court does not have jurisdiction in respect of property held outside the jurisdiction (see *British South Africa Co v Companhia de Mocambique* [1893] AC 602 and also Nygh P E, Conflict of Laws in Australia, 6th Ed, Butterworths, Sydney 1995) but it is able to make an order *in personam (see In the Marriage of Perry* (1978) 3 Fam LN 77).

[15] Lueg, Corinna, Valuation of Superannuation for Family Law, 9th National Family Law Conference, July 2000, pp36-37.

[16] See Part 5 of the Family Law (Superannuation) Regulations 2001.

[17] The valuation of partially vested accumulation plans will also proceed along the same lines as the valuation of defined benefit plans.

[18] Section 17A *Superannuation Industry (Supervision) Act 1993*.

- each individual trustee of the fund must be a fund member (where the trustee is a corporate trustee, each director of the corporate trustee must be a fund member);
- each member of the fund must be a trustee (where the trustee is a corporate trustee, each member of the fund must a director of the corporate trustee);
- no member of the fund can be an employee of another member, unless those members are related; and
- no trustee can receive any form of remuneration for trustee services.

Retirement savings accounts are governed by the *Retirement Savings Accounts Act 1997* and small superannuation accounts are governed by the *Small Superannuation Accounts Act 1995*. Retirement savings accounts are designed to be a simple, low cost and low risk savings product as an alternative to superannuation funds. They are aimed at those with small amounts of superannuation or with transient working patterns. They do not have a trust structure but are in the form of capital guaranteed account but attract the same taxation treatment on exit as the traditional forms of superannuation.

Small superannuation accounts are part of the Superannuation Accounts Holding Reserve (SHAR) which was created to receive employer contributions under the superannuation guarantee scheme. It is administered by the Tax Office and amounts deposited are not superannuation contributions. They do not attract superannuation contributions tax. Interest is paid on amounts up to $1,200 and no interest is payable on amounts exceeding $1,200. Employers may claim contributions as deductions for income tax purposes but again only up to $1,200. This is designed as a disincentive to accumulating significant sums in the SHAR.

A partially vested accumulation interest is one where it operates in the same way as a fully vested accumulation interest but there are particular vesting points, for example at 5 years, 10 years and 15 years where further value is added to the accumulated sum. There is no set rule for the vesting points but these points are illustrative of the type of plan where there is partial vesting. Thus, where a person is a member of a partially vested accumulation plan, accumulations are made in the usual manner but there are

"bonus" payments at the prescribed vesting points. They are typically company run plans and are designed to provide an incentive for the employee to remain with the company. The operation of these plans in all other respects is the same as a fully vested accumulation plan.

A percentage only interest is one which is defined to be a percentage only interest for purposes of the FL Superannuation Act.[19] These have yet to be fully listed but will typically be judges and parliamentary plans where the vesting scales are extreme making a "smooth" actuarial valuation more difficult. The only interest defined as a percentage only interest is the Commonwealth judicial pensions plan.

Defined benefit interests are those where a benefit is paid by reference to salary at the date of termination or retirement, average salary, a specified amount or specified conversion factors.[20]

A convenient rule of thumb to guide practitioners is that public sector employees, employees of large corporations (especially those that were at one stage government owned) as well as some corporate executive plans will be defined benefit plans or partially vested accumulation plans. Judges pensions and parliamentary superannuation will be treated separately. Industry or award plans, master trusts, self managed funds and public offer plans will typically be accumulation plans. However, the trust deeds will be critical in determining into which category the superannuation interest will fall.

What Type of Interest is it?

It will be important for practitioners to be able to identify the type of superannuation which is in issue. The path through the new scheme depends on the type of superannuation interest. Section 90MD of the FL Superannuation Act and regulation 5 of the FL Regulations have the following definitions:

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[19] Section 90MD of the *Family Law Act 1975* inserted by the FL Superannuation Act and Regulation 3 of the *Family Law (Superannuation) Regulations 2001*.

Eligible superannuation plan means any of the following:
(a) a superannuation fund within the meaning of the SIS Act;
(b) an approved deposit fund within the meaning of the SIS Act
(c) an RSA;
(d) an account within the meaning of the *Small Superannuation Accounts Act 1995*.

Superannuation interest means an interest that a person has as a member of an eligible superannuation plan, but does not include a reversionary interest.

5. (1) Subject to subregulation (2), a **defined benefit interest** is a superannuation interest, or component of a superannuation interest, that a member spouse has in relation to an eligible superannuation plan, being an interest in respect of which the member spouse is entitled, when benefits in respect of the interest become payable, to be paid a benefit defined that is, or may be, defined by reference to one or more of the following:
(a) the amount of:
   (i) the member spouse's salary at the date of the termination of the member spouse's employment, the date of the member spouse's retirement, or another date; or
   (ii) the member spouse's salary averaged over a period before retirement;
(b) a specified amount;
(c) specified conversion factors.

(2) A superannuation interest, or a component of a superannuation interest, is not a **defined benefit interest** for this Part if the only benefits payable in respect of the interest that are defined by reference to the amount or factors mentioned in subregulation (1) are benefits payable on death or invalidity.

Accumulation interest means a superannuation interest that is not a defined benefit interest or a small superannuation accounts interest.

Superannuation has many forms. The simplest form is also the most common form. Accumulation plans account for 86% of memberships[21]. These plans consist of amounts contributed by the employee, contributions by the employer, interest earned and a deducted administration fee[22]. Funds are thus accumulated (hence the name accumulation plan, although they are sometimes referred to as defined contribution

[20] Regulation 5 of the *Family Law (Superannuation) Regulations* 2001 and see regulation 1.03 of the *Superannuation Industry (Supervision) Regulations*.
[21] APRA 2000, Superannuation Trends, Sept Quarter
[22] McIlroy, John, *Superannuation Explained Simply*, Wrightbooks, 1994, pp123-4.

plans) and the employee receives the sum accumulated (subject to tax) when he or she meets a condition of release[23].

The remaining 14% of superannuation memberships are hybrid plans and defined benefit plans. These have always been the difficult part of any attempt at superannuation reform and to ignore them would not provide universal coverage. To include them naturally makes the proposals much more complex because their valuation is problematic and their division at the time of court order raises constitutional difficulties.

Constitutional Issues

A convenient place to start in relation to the constitutional underpinnings of the *Family Law Act 1975* is the accepted interpretation of the marriage power. To withstand constitutional challenge, a law relying on the marriage power for validity must demonstrate a sufficient connection with the marriage[24]. In *Re Lambert; Ex Parte Plummer*[25], Gibbs J said:

> The crucial question, however, is whether the legislation creates, defines or declares rights or duties that arise out of, or have a close connection with, the marriage relationship. (at 75,691)

Although Gibbs J described the connection as "close", later qualified as being "sufficient"[26], the difficulty faced in drafting the amendments to the *Family Law Act 1975* is to ascertain the sufficiency of the connection. It is clear that "[i]t is not enough that the law incidentally touches upon marriage, or that Parliament has seized on the fact of marriage as a justification for the enactment of a law which really deals with some other topic."[27] The connection must show a reasonable proportionality

[2323] A condition of release is met when there is a nil cashing restriction. See generally, Division 6.3 fo the SIS Regulations

[24] *Fountain v Alexander* (1982) FLC ¶91-218. An earlier, much narrower, interpretation which relegated the marriage power to regulating little more than the formation of marriage, no longer enjoys any currency.

[25] (1980) FLC ¶90-904.

[26] *Fountain v Alexander* (1982) FLC ¶91-218.

[27] *Gazzo v Comptroller of Stamps (Vic*) (1981) FLC ¶91-101 at 76,719 and see more recently *Cui v Li and Ors* [2001}NSWSC 90.

between the nature and strength of the connection and the relevant operation of the law[28]. It is proportionality which is at the heart of constitutional considerations.

In the superannuation amendments then, the question is whether an amendment to split a superannuation interest is sufficiently connected to the marriage relationship. In other words, is the law to split superannuation in the form in which it is enacted in reasonable proportion to the circumstances arising out of the marriage. The new super splitting laws will enable the splitting of a superannuation interest of one, or both, of the parties to the marriage where the splitting is required because of the circumstances arising out of the marriage ie typically because the marriage relationship has broken down and the splitting of superannuation is required to do justice and equity between the parties. Anything beyond this, runs the risk that the law is simply seizing on the fact of marriage as a justification for its enactment. There are some reported instances of cases where the court has been called upon to determine questions where the parties happen to be husband and wife.[29]

The changes will give the court jurisdiction over the subject matter and the power to bind third party trustees to the terms of the order made by the court. The jurisdiction will be achieved by extending the meaning of "matrimonial cause" in section 4 whereby a superannuation interest is to be treated as property for the purposes of paragraph (ca) of the definition of matrimonial cause.[30] Paragraph (ca) provides the basis for the property jurisdiction as "being proceedings between the parties to a marriage with respect to the property of the parties to the marriage or either of them, being proceedings arising out of the marital relationship."

Treating superannuation as property has a number of consequences. First, the court will have jurisdiction over all superannuation whenever acquired.[31] This will include superannuation acquired prior to the marriage as well as that which is acquired after separation. The assessment made by the court as to contributions, however, will be the same as for other property, relying on the existing wording of s79. The cases on

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[28] *Re Cook and Maxwell JJ; Ex Parte C* (1985) FLC ¶91-619

[29] *R v Ross Jones; Ex Parte Beaumont* (1979) 114 CLR 504 and *Cui v Li and Ors* [2001] NSWSC 90.

[30] Section 90MC of the *Family Law Act 1975* inserted by the *Family Law Legislation Amendment (Superannuation) Act 2001*.

[31] *Kowalski and Kowalski* (1993) FLC ¶92-342.

initial contribution[32] as well as contributions to the acquisition of property after separation[33] will apply. The superannuation will also be available along with other property to make any further adjustments, in accordance with ss75(2), after the contributions step.

Second, treating superannuation as property for the purposes of the definition of matrimonial cause provides complete discretion for a court to determine whether to split superannuation and if so, the proportions of the split. However, the types of orders the court may make are prescribed by the terms of the new super splitting laws because splitting a superannuation interest has implications for trustees and administrators. Thus the new laws require that any splitting must be made in accordance with the requirements of the new super splitting laws.[34] In effect, the new super splitting laws provide a complete set of rules for the way in which a split of superannuation will occur but not the proportions. The proportions are completely within the discretion of the court exercising jurisdiction.[35]

Valuation

A preliminary point is to decide whether the superannuation is in the accumulation phase or in the payment phase.[36] Valuation of an accumulation interest as it is being accumulated is governed by regulation 31 of the *Family Law (Superannuation) Regulations 2001* (the FL (Superannuation) Regulations). This regulation has a number of components to it. The starting point is the value of the interest provided to the member in the member statement. Where a value is required which is between two member statements, a formula is provided as follows (simplified for the purposes of this paper):

$$V_1 + \frac{(V_2 - V_1) \times X}{D}$$

[32] See, for example, *Bremner and Bremner* (1995) FLC ¶92-560.
[33] See, for example, *Ferraro and Ferraro*, (1992) FLC ¶92-335.
[34] See section 90MS of the *Family Law Act 1975* inserted by the *Family Law Legislation Amendment (Superannuation) Act 2001.*
[35] Section 90MS of the *Family Law Act 1975* inserted by the *Family Law Legislation Amendment (Superannuation) Act 2001*.
[36] Regulation 6, 7 and 8 of the *Family Law (Superannuation) Regulations 2001*.

Where V_1 = Value at first valuation date
V_2 = Value at 2nd valuation date
X = Number of days up to the valuation point
D = Number of days in the valuation period

The formula provides a mechanism whereby a valuation between member statements can be obtained by calculating the mean value in accordance with the formula. Further provision is made where there is only one member statement, such as for a new member.[37] The purpose of this regulation is to obtain an amount equivalent to or approximating the withdrawal benefit which is the total amount of the benefits that would be payable if the member voluntarily ceased to be a member.[38] This value is reported to members.[39]

Valuation of a defined benefit interest in the accumulation phase is governed by regulation 29 of the FL (Superannuation) Regulations, which requires that the valuation proceed in accordance with Schedule 2 of the FL (Superannuation) Regulations. This schedule lifts the "actuarial veil" that was the cause of so much controversy before the Senate Committee. Schedule 2 provides for the calculation of the present day value where the benefit is payable as a lump sum only[40], where the benefit is payable as a pension only[41] and where the benefit is payable as a combination of lump sum and pension[42]. The calculations proceed by way of a series of calculations (simplified again for the purposes of this paper):

$$A \times f_{y+m}$$

Where:

A is the product of the member spouse's accrued benefit multiple for a lump sum and the salary figure on which benefits in respect of the interest, at that date, would be based, assuming that the member spouse were eligible to retire at that date.

f_{y+m} is the lump sum valuation factor taken from the table in clause 4, schedule 2 where the remaining term to retirement is in complete years.

[37] Regulation 31(4) of the *Family Law (Superannuation) Regulations 2001*.
[38] Regulation 1.03, *Superannuation Industry (Supervision) Regulations.*
[39] Regulation 2.23, *Superannuation Industry (Supervision) Regulations*.
[40] Part 2 of Schedule 2 of the *Family Law (Superannuation) Regulations 2001*.
[41] Part 3 of Schedule 2 of the *Family Law (Superannuation) Regulations 2001*.
[42] Part 4 of Schedule 2 of the *Family Law (Superannuation) Regulations 2001*.

Where the remaining term to retirement includes a number of complete months as well as complete years, the lump sum valuation factor is derived by means of a linear interpolation represented by the following formula:

$$\frac{\left(f_y \times (12 - m)\right) + \left(f_{y+1} \times m\right)}{12}$$

Where:

f_y is the lump sum valuation factor mentioned in clause 4 of Schedule 2 that applies at the relevant date to the term remaining in complete years until the member spouse reaches the member's retirement age.

m is the number of complete months of the remaining term that are not included in the remaining complete years at the relevant date.

f_{y+1} is the lump sum valuation factor mentioned in clause 4 of this Schedule that applies to the remaining term at the completion of the next year after the year mentioned in the definition of the factor f_y.

When applied in sequence, the calculation will yield the actuarial valuation given the assumptions underlying the contingent value factors. Valuation of superannuation is a separate paper on its own but it is sufficient for the purposes of this paper to note that the valuation technique applied to defined benefit plans will unearth the unvested value of a defined benefit. Valuation of superannuation in the payment phase is designed to identify a capital sum underlying the income stream, which may be used in adjusting other property. However, the court is able to split the income stream on a percentage basis.

The assumptions underpinning valuation derive from a public sector scheme covering white collar workers. This will not suit all superannuation plans. For example, some plans will cover different classes of employees where exit rates differ. Where the method and factors yield a result which is not in accord with the underlying plan design, separate factors can be prepared by the trustees for approval by the Attorney-General.[43] The instrument approved by the Attorney-General is a disallowable instrument and is governed by section 46A of the *Acts Interpretation Act 1901*.

[43] Regulation 38 of the *Family Law (Superannuation) Regulations 2001*

Splitting the interest

Once the valuation has been derived, the action then turns to much more familiar ground for family lawyers - decide on the proportions to be allocated between the parties.

Court Orders

For court orders, splitting is done in the context of the section 79 powers of the court exercising jurisdiction. Subsection 90MS(1) states:

> (1) In proceedings under section 79 with respect to the property of the spouses, the court may, in accordance with this Division, also make orders in relation to the superannuation interests of the spouses.
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> Note 1: Although the orders are made *in accordance with* this Division, they will be made *under* section 79. Therefore, they will be generally subject to all the same provisions as other section 79 orders.
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> Note 2: Sections 71A and 90MO limit the scope of section 79.

The effect of this provision is to confirm that the court is making its order in relation to superannuation pursuant to section 79. The opening words of s.90MS say that and it is confirmed by the note to s.90MS.[44]. Jurisdiction is derived from the proceedings rather than the property and the court therefore has jurisdiction over all superannuation whenever acquired. As the Full Court said in *Kowalski and Kowalski*:

> once a marriage has been celebrated between the parties, the entire relationship between the parties, whether arising out of contributions before, during or after the formal tie of marriage was entered into or dissolved, falls within the ambit of Part VIII of the Family Law Act[45] (see p 79,630).

Thus, the court exercising jurisdiction is to look at the contributions to the acquisition, conservation and improvement of the superannuation and can make any further adjustment having regard to the factors set out under section 75(2). Part VIIIB introduces an important qualification on the making of a section 79 order in that the making of an order which involves the splitting of a superannuation interest must follow the provisions set out in Part VIIIB.

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[44] Notes do not form part of the text of the Act - s13 of the *Acts Interpretation Act 1901*.

The court will be able to make an order to split superannuation in whatever proportion the justice and equity of the case requires including not to split superannuation but to alter interests in other property by way of adjustment. Thus if there are current housing needs, especially for children, the court may make an order giving superannuation to one parent and the house to the other parent to provide for the housing needs of that parent and the children.

When the court makes an order to split a superannuation interest, the regime contained in Part VIIIB requires the court to value the interest in accordance with any method provided by regulations for determining the value of the interest[46] and to make one of three types of orders:

- For non percentage-only interests, an order which has the effect of giving the non-member spouse an entitlement to be paid an amount calculated in accordance with the regulations and reducing the entitlement of member correspondingly (for convenience, these can be referred to as **Type A** orders);
- For non percentage-only interests, an order which has the effect of the giving the non-member spouse an entitlement to be paid a specified percentage of a splittable payment and reducing the entitlement of member correspondingly (**Type B** orders); and
- For percentage only interests, an order which has the effect of the giving the non-member spouse an entitlement to be paid an amount calculated in accordance with the regulations but by reference to a percentage specified in the order and reducing the entitlement of member correspondingly (**Type C** orders).

The court exercising jurisdiction is also able to make such other orders as the court thinks necessary for the enforcement of any of its splitting orders.

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[45] *Kowalski and Kowalski* (1993) FLC ¶92-342 at p79,630.
[46] S.90MT(2) of the *Family Law Act 1975* inserted by the *Family Law Legislation Amendment (Superannuation) Act 2001*.

The new super splitting laws do not prescribe the circumstances in which the three types of order can be used. However, the effect of each order is carefully set out in s.90MT(1). The indications for the use of a particular order are derived from its effect.

Type A orders have the effect of giving to the non-member spouse an amount calculated in accordance with the regulations. However, before a type A order is made, the court making the order must allocate a base amount to the non-member spouse.[47] The effect of type A orders makes them most appropriate when superannuation is in the growth phase. The reason for this is because its effect is to set aside a lump sum amount (the "base amount") for payment to the non-member spouse when the superannuation becomes payable. The lump sum amount can be determined at the time of settlement in one of two ways. First, it can be determined by applying a percentage to the overall value of the superannuation, that percentage being determined by the court in the exercise of its discretion. Alternatively, it can be determined simply by allocating an identified amount from the overall value of the superannuation. Either will achieve the same result of determining a lump sum, or base amount to be allocated to the non-member spouse.

The type B order will be most appropriate when the superannuation is in the payment phase. Under a type B order, a court is able to make an order which has the effect that whenever a splittable payment becomes payable, the non-member spouse is entitled to be paid a specified percentage of the splittable payments made to the member. Making this order in the growth phase will incorporate all post order accumulations in the percentage split. However, where superannuation is in payment, a simple percentage split will yield an outcome which spits the income stream as well as any future lump sums in accordance with the percentage split. The member's entitlement to the payment is reduced accordingly.

The type C order must be used for percentage-only interests. Percentage only interests are prescribed by the regulations, and the only interest that is presently prescribed is the Commonwealth judicial pension scheme (s.90MD and r.3). The

explanatory memorandum states that the purpose of prescribing interests as percentage-only interests is because that method of splitting is the only appropriate and equitable method given the vesting characteristics of those interests. In the words of the explanatory memorandum "the amount of the benefits increases exponentially on the occurrence of a specified event".

A type C order is an order which has the effect of the giving the non-member spouse an entitlement to be paid an amount calculated in accordance with the regulations but determined by reference to a percentage specified in the order. Again the member's entitlement is correspondingly reduced. R.26 provides the key to the operation of a type C order. It provides:

> The amount that the non-member spouse is entitled to be paid in respect of a splittable payment that becomes payable in respect of the superannuation interest is:
>
> $$\left(\frac{\text{Accrued benefit multiple at separation}}{\text{Accrued benefit multiple at payment}} \times \boldsymbol{X}\right) \times \boldsymbol{SP}$$
>
> where:
>
> ***Accrued benefit multiple at separation*** is the member spouse's accrued benefit multiple, as defined in the governing rules of the eligible superannuation plan in which the superannuation interest is held, at the date when the member spouse and non-member spouse separated or, if there have been 2 or more separations, at the date of the most recent separation
>
> ***Accrued benefit multiple at payment*** is the member spouse's accrued benefit multiple, as defined in the governing rules of the eligible superannuation plan in which the superannuation interest is held, at the date when the splittable payment becomes payable in respect of the superannuation interest.
>
> ***X*** is the percentage specified in the agreement.
>
> ***SP*** is the amount of the splittable payment.

The effect of this formula for the splitting of superannuation where the interest is a percentage-only interest is based on the concept of the accrued benefit multiple. The accrued benefit multiple is the multiple which is used to actuarially calculate the

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[47] S.90MT(4) of the *Family Law Act 1975* inserted by the inserted by the *Family Law Legislation*

accrued liability for interests within the plan. The explanatory statement for the Regulations explains it in the following terms:

> Regulation 26 provides for the entitlement of a non-member spouse in respect of each splittable payment that becomes payable in respect of a percentage-only interest that is subject to a percentage split under a superannuation agreement that applies for the purpose of subparagraph 90MJ(1)(b)(i) of the Act. The entitlement is, broadly speaking, a percentage of each splittable payment that reduces, in accordance with the formula in the provision, over time, as the period of the member spouse's post-separation membership of the plan in which the interest is held increases.

In other words, because the benefit multiple increases over time, the value of the interest will increase. However, the multiple that has accrued to the time of separation becomes a fixed reference point, reducing the percentage of the overall superannuation to be split.

Superannuation Agreements

Splitting can also be achieved by means of a superannuation agreement.[48] A superannuation agreement forms part of a financial agreement[49] and therefore is governed by the requirements of binding financial agreements, including the requirement that it be made in writing and each party to the agreement receiving separate legal advice[50]. To create a split of superannuation, the agreement must specify an amount as a base amount, a method to calculate the base amount or a percentage to apply to all splittable payments[51].

Exceptions

Some interests are not splittable[52]. Payments made to members on compassionate grounds, grounds of hardship, permanent incapacity (or temporary incapacity longer

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Amendment (Superannuation) Act 2001.

[48] Division 2, Part VIIIB of the *Family Law Act 1975* inserted by *Family Law Legislation Amendment (Superannuation) Act 2001.*

[49] Section 90MH of the *Family Law Act 1975* inserted by the *Family Law Legislation Amendment (Superannuation) Act 2001.*

[50] Section 90L of the *Family Law Act.*

[51] Section 90MJ(1)(c) of the *Family Law Act 1975* inserted by the *Family Law Legislation Amendment (Superannuation) Act 2001*

[52] Section 90ME(2) of the *Family Law Act 1975* inserted by the *Family Law Legislation Amendment (Superannuation) Act 2001* and Part 2 of the *Family Law (Superannuation) Regulations 2001*.

than 2 years[53]), payments pursuant under the *Small Superannuation Accounts Act 1995* or payments to children are all unsplittable payments. In addition, where a new interest is created in the name of the non-member spouse[54], any payments that would be splittable by virtue of the court order or agreement after the creation of the new interest are also not splittable (see the definition of spent payment split[55]).

Flagging a Superannuation Interest

An alternative to a splitting order or agreement is to flag the superannuation interest. The effect of placing a flag on the superannuation interest is to prohibit the making of a splittable payment by the trustee.[56] In many ways, a payment flag acts like a statutory injunction. In the case of court orders, where the trustee fails to observe the terms of the order, the trustee will be subject to the penalties for breach of an order.[57] In the case of agreements, a penalty of 50 penalty units is prescribed[58] (250 penalty units applies to bodies corporate).[59]

Practitioners may ask what are the appropriate circumstances for considering the imposition of a flag. The use of the flag will postpone the time for the valuation and split of a superannuation interest until the flag is lifted. Before making an order to flag a superannuation interest, the court may take into account any matter it considers relevant and in particular, the likelihood that a splittable payment may soon become payable.[60] In the interests of certainty for the parties, it is suggested that a flag be used where the interest is a defined benefit or a partially vested accumulation interest and a condition of release is imminent. In addition, the imposition of a flag by agreement or consent order is advisable only where the relationship between the

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[53] Provided the payments do not reduce the member spouse's ultimate benefit.
[54] The exception will also apply where an amount is rolled out of the member spouse's fund to a fund for the benefits of the non-member spouse.
[55] Section 90ME(2) of the *Family Law Act 1975* inserted by *Family Law Legislation Amendment (Superannuation) Act 2001.*
[56] Section 90ML(4) (agreements) and section 90MU(1) (orders) of the *Family Law Act 1975* inserted by the *Family Law Legislation Amendment (Superannuation) Act 2001.*
[57] Section 90MZD of the *Family Law Act 1975* inserted by *Family Law Legislation Amendment (Superannuation) Act 2001.*
[58] Section 90ML(4) of the *Family Law Act 1975* inserted by *Family Law Legislation Amendment (Superannuation) Act 2001*
[59] A penalty unit is $110 - see section 4AA of the *Crimes Act 1914*.
[60] Section 90MU(2) of the *Family Law Act 1975* inserted by *Family Law Legislation Amendment (Superannuation) Act 2001*

separating parties is relatively stable. This avoids the difficulties that may arise should the relationship deteriorate at a later point in time when the flag is to be lifted.

Where a flag has been imposed by agreement, it can be lifted by agreement. The effect of a flag lifting agreement is twofold. First, it will lift the prohibition on payments and second it will identify a split of the superannuation. In this way, it has the same effect as a splitting agreement and thus section 90MJ is drafted to cover both types of agreements. Where some time has passed since the agreement to flag the superannuation interest and the parties cannot agree to lift the flag, an application may be made to the court pursuant to section 90K(1)(f) of the *Family Law Act*. That provision states:

> A court may make an order setting aside a financial agreement or a termination agreement if, and only if, the court is satisfied that:
> …
> (f) a payment flag is operating under Part VIIIB on a superannuation interest covered by the agreement and there is no reasonable likelihood that the operation of the flag will be terminated by a flag lifting agreement under that Part;

Where the flag is imposed by court order, the court has the power to lift the flag and make a splitting order under section 90MT.

Creation of a new accumulation interest

One of the benefits of the new super splitting laws is that it enables the creation of a new interest in superannuation. However, for reasons outlined earlier, the creation of a new interest out of a defined benefit interest or a partially vested accumulation interest would infringe the just terms requirement of the Constitution. So the option of creating a new interest will apply only to fully vested accumulation plans. The marriage and matrimonial causes powers do not provide sufficient connection between the creation of a new interest and marriage. Thus other heads of power have been called in aid. The corporations and pensions powers underpin the superannuation regulatory regime[61] (together with taxation powers) and the legislation

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[61] See the definition of "constitutional corporation" and "old age pension" in section 10 and their application in section 19 of the *Superannuation Industry (Supervision) Act 1993*.

governing the creation of a new interest is therefore contained in amendments to the SIS Amendment Regulations. It should be remembered, however, that this arrangement applying to fully vested accumulation interests will cover the majority of interests.

Diagram 1 outlines how this is achieved. When the trustee receives a copy of the court order or superannuation agreement in respect of an interest in a regulated superannuation fund or an approved deposit fund, the trustee must give to both parties a notice, a "payment split notice", within 28 days after the operative time of the agreement or in the case of a court order either the end of the 28 days after the operative time or 28 days after the receipt of the order, whichever is the later.[62]

The non-member may elect to have an interest created in the fund[63] unless the governing rules of the fund prevent that course of action. The notice must be made within 28 days of the payment spit notice and be signed, dated and provide the name, date of birth and postal address of the non-member spouse (soon to become a member). The trustee is obliged to create a new interest when requested unless a request to roll over the interest of the non-member spouse was made prior to the request to create the new interest or the governing rules of the fund do not allow the creation of a new interest.[64] The value of the new interest is the value of the base amount plus adjustments (if any) less any payments under a payment split (if any).[65] The preservation components of the interest are taken to be in the same proportions as the member's interest.[66] Alternatively, the trustee may create a new interest without a request.[67]

The alternative course of action is to roll over or transfer the transferable benefits to another fund. The transfer request may be made either by the non-member or, in the case of a self managed superannuation fund, the member.[68] Where there is no request

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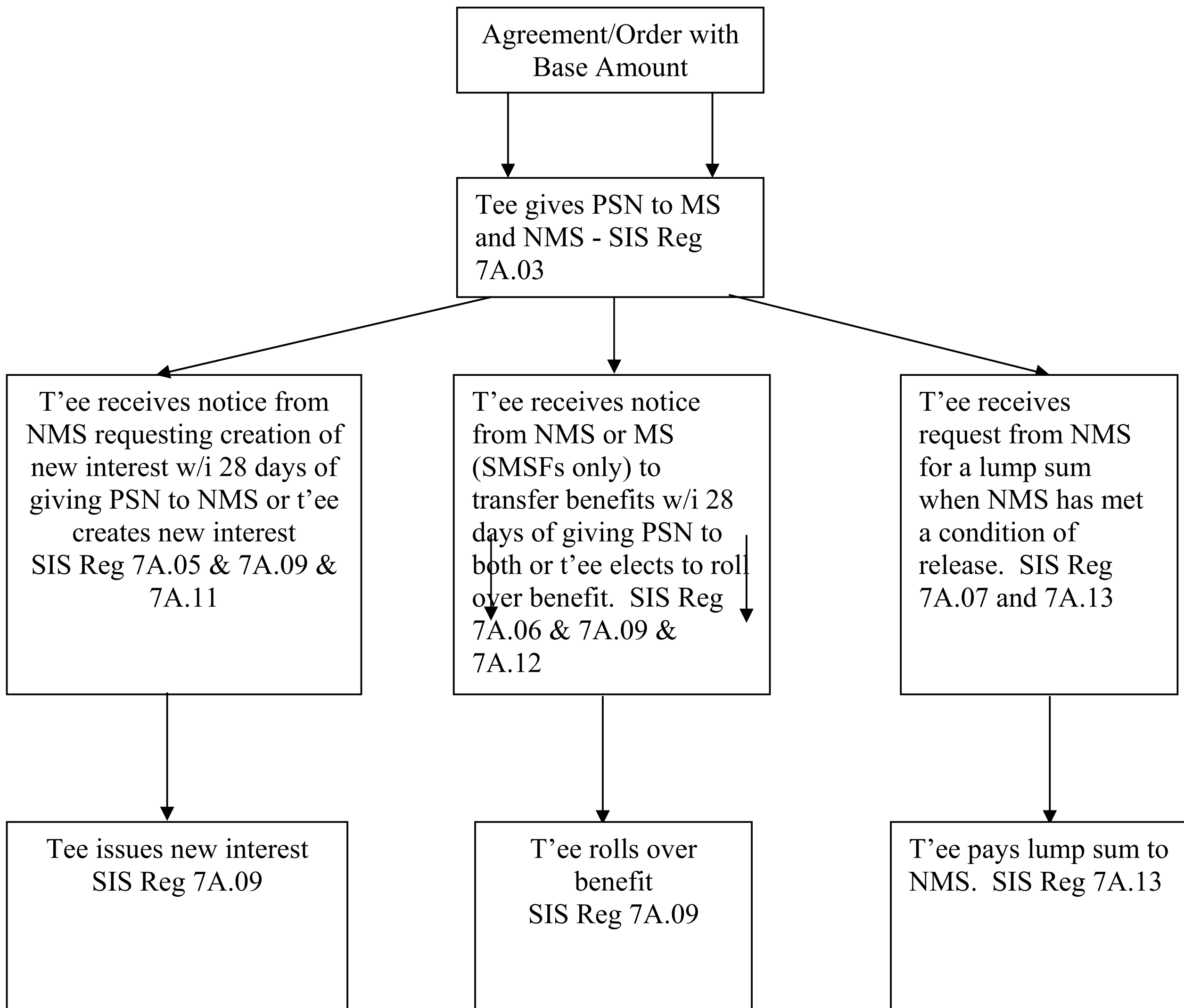
[62] Regulation 7A.03 of the SIS Amendment Regulations.
[63] Regulation 7A.05 of the SIS Amendment Regulations.
[64] Regulation 7A.09 of the SIS Amendment Regulations
[65] Regulation 7A.11 of the SIS Amendment Regulations
[66] Regulation 7A.11(6) and (7) of the SIS Amendment Regulations
[67] Regulation 7A.10 of the SIS Amendment Regulations.
[68] Regulation 7A.06 of the SIS Amendment Regulations

to transfer, the trustee may transfer the transferable benefit[69] to another fund or an eligible rollover fund. The preservation components of the interest are again taken in the same proportions as they exist in the member's interest.[70] This course of action is most likely to be the case where the plan is an occupationally linked plan which has employees of a particular occupation. Retaining members who are not employed within the particular occupational group for which the plan operates may present difficulties for the benefit design of the plan. Thus transfer of interests from these memberships will be the preferred course of action. This may also be preferred where the non-member spouse has other superannuation and wishes to consolidate the holdings.

[69] Regulation 7A.10 of the SIS Amendment Regulations.
[70] Regulation 7A.12 of the SIS Amendment Regulations

DIAGRAM 1: CREATION OF A NEW INTEREST (ACCUMULATION PLAN)



Defined benefit interests & partially vested accumulation interests

Diagram 2 shows the steps for dealing with defined benefit interests and partially vested accumulation interests after the court has made its splitting order or the parties have made a superannuation agreement. Using court orders to illustrate, the court identifies a base amount in making a splitting order which becomes the amount to be paid to the non-member spouse. The non-member spouse is entitled to be paid the amount being the base amount and any adjustments made until the interest is released to the member.[71] The adjustments to the base amount will depend on how the member's interest grows. In general, where the member's interest grows at a particular rate, the base amount is intended to grow at the same rate.[72] While the base amount remains part of the member's superannuation interest, the adjustments only apply to that amount of the member's interest which represents the base amount. This means that the member is able to make further contributions without further enriching the amount ultimately to be paid to the non-member spouse.

It is important to be reminded that, in contrast to accumulation interests, the creation of a new interest in a defined benefit plan would contravene the just terms requirement in the Constitution. For this reason, the new scheme is constructed so that the split only occurs on payment, which is typically when a condition of release is satisfied.[73] One of the consequences of this is that the decision-making for meeting the condition of release lies with the member. For example, the member's account may have an adjusted base amount attached to it requiring the trustee to pay the non-member spouse the adjusted base amount when a payment becomes payable to the member. The decision as to when superannuation is to be taken, being largely in the hands of the member, the release of the funds can be postponed until at least age 65. It can be deferred beyond that where the member is gainfully employed for more than 10 hours per week.[74] Postponement of compulsory cashing can be deferred beyond age 70 where the member is gainfully employed for more than 30 hours per week.[75]

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[71] Section 90MT(1)(a)(i) of the *Family Law Act 1975* inserted by *Family Law Legislation Amendment (Superannuation) Act 2001*

[72] Regulation 48 of the *Family Law (Superannuation) Regulations 2001*.

[73] See also the definition of splittable payment in proposed section 90ME

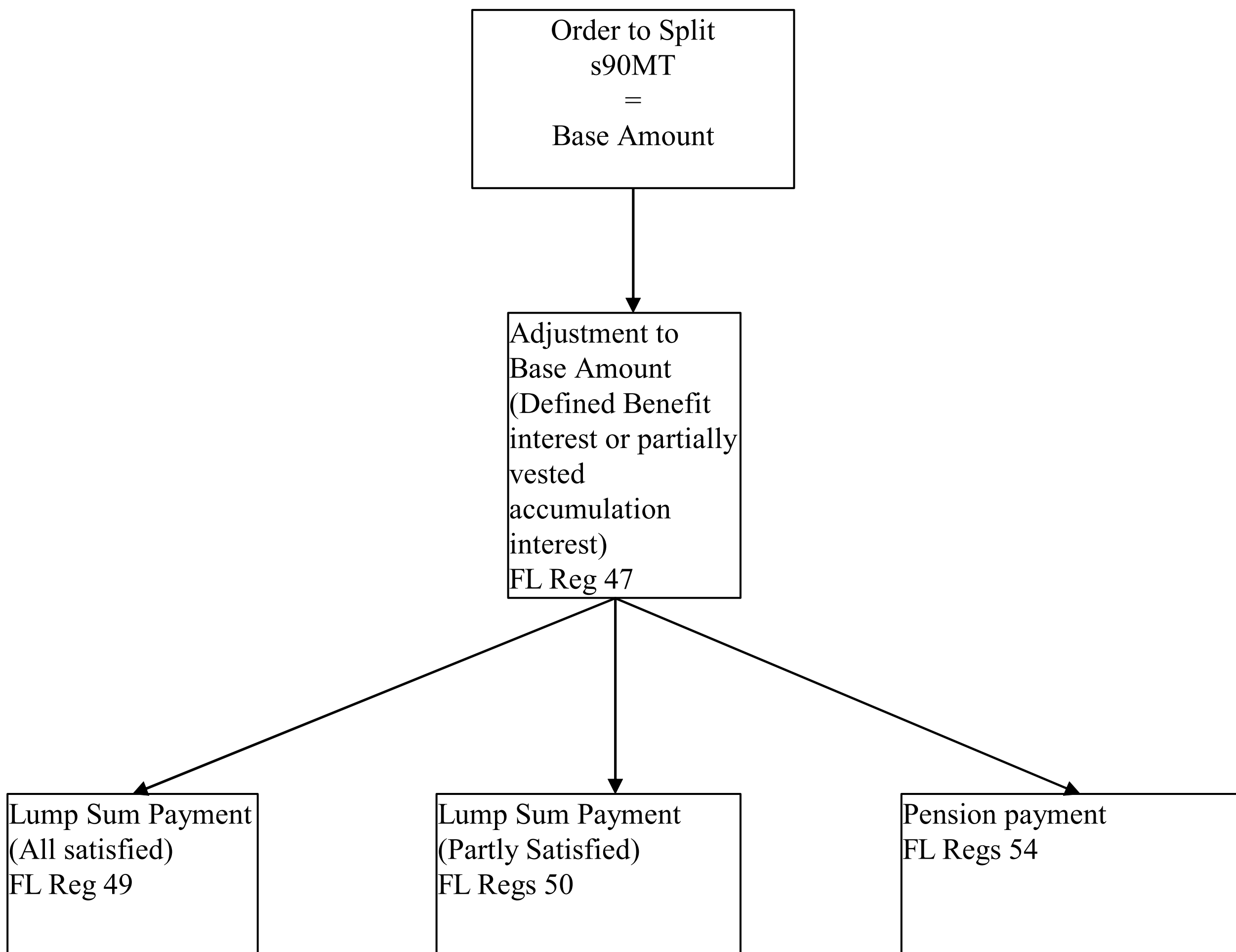
[74] Regulation 6.21 and definition in Regulation 1.03(1) of the SIS Regulations.

What happens on release of funds is governed by regulation 49 of the FL (Superannuation) Regulations. The general rule is that to the extent that the adjusted base amount payable to the non-member spouse can be satisfied by a lump sum, it must be done in that way.[76] Complexity arises where there is insufficient lump sum to satisfy the adjusted base amount. Or to put it another way, there is a capital sum in the form of the adjusted base amount and the only means the member has to satisfy the amount due and payable to the non-member is by way of an income stream. That is the purpose of regulation 50 of the FL (Superannuation) Regulations. To put it at its most simple, Regulation 50 works out what the proportion of the income stream should be paid to the non-member spouse given that some lump sum may have been paid.

[75] Regulation 6.21 and definition in Regulation 1.03(1) of the SIS Regulations.
[76] Regulation 49 of the Family Law (Superannuation) regulations 2001.

Defined benefit splits and partially vested accumulation splits are represented by the following diagram:

Diagram 2: Defined Benefit Interests and Partially Vested Accumulation Interests



Conclusion

The purpose of this paper has been to briefly describe the changes in the new super splitting laws. The new scheme represents the outcome or resolution of tensions between four competing principles – equity, simplicity, certainty and administrative convenience. The proposals in the reform package involve a series of steps where the policy development of each of those steps required a judgement to be made as to whether, for example, a degree of complexity should be tolerated for greater equity. Or whether absolute equity should give way to administrative convenience. Some will make the judgement one way saying that the Act and Regulations are too difficult to understand and it is of no use to have this degree of complexity because it will not be understood. But to simplify the proposals will see a loss of equity as between spouses. Any change to the proposals will re-arrange the delicate balance between the principles. If one is to advocate less complexity, the consequences of that course of action on the distribution of equity between the parties must also be articulated.

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