

SuperViews

From the office of the
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SAS Trustee
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Splitting of a superannuation interest on marriage breakdown

Introduction

From 28 December 2002, Commonwealth Family Law legislation provides for superannuation benefits to be treated as *property* that can be divided or split on marriage breakdown. The legislation applies to all superannuation funds and legally married couples except where information is being requested for the purposes of negotiating a pre-nuptial agreement. The legislation does not apply to couples in a de facto relationship.

This article provides a summary of the complex Family Law provisions, commonly known as the *splitting laws* as they apply to current members of the defined benefit STC schemes — the State Authorities Superannuation Scheme (SASS), State Superannuation Scheme (SSS) and Police Superannuation Scheme (PSS). Different rules apply to the splitting of a benefit in payment ie. a pension being paid to a retired scheme member.

The splitting laws allow for a superannuation *interest* to be divided by either:

- agreement between the parties to a marriage breakdown, or
- by Court Order.

A superannuation fund must act on a valid agreement or Court Order.

As explained below, there are 3 basic steps in the process of splitting a superannuation interest:

- information gathering,
- benefit *flagging*, and
- benefit splitting.

Access to information from superannuation funds

So that a superannuation interest may be valued and split fairly between the marriage partners, it is necessary for them (or the Family Court on their behalf) to know the current amount of the benefit accrued by a member in their superannuation fund. Other details are also required, such as when a benefit becomes payable to a scheme member under the fund's rules. Where both marriage partners have accrued superannuation benefits, it will be necessary for them to gather information about both accounts.

To facilitate this, the splitting laws allow persons other than the scheme member to request and be provided with information about a member's superannuation interest.

Who may request information?

Either or both marriage partners may apply to a fund for information about a member's superannuation interest. It is not necessary for the parties to be separated or for divorce proceedings to have commenced. Where the applicant is the member's spouse (called the *non-member spouse*), the fund cannot:

- tell the member that the request for information has been received from the member's spouse, or
- give out the member's address to the spouse.

A request for information can also be made by a person intending to enter into a superannuation agreement with the scheme member before marriage (such as a pre-nuptial agreement).

A request for information for family law purposes must be submitted on a special form — known as *Form 6*. This

form is available from a variety of sources including your legal adviser, the Family Law Court web site, and State Super's Customer Service. Generally, the necessary form would be provided to you by your legal adviser.

A request for information must be accompanied by an application fee — currently \$275 (including GST) for information about a current scheme member's benefit and \$110 (including GST) for information about a deferred benefit of a former contributory member.

What information is provided?

The range of information that must be provided by a fund is set out in the provisions of the Family Law legislation. It is based on the scheme member's superannuation interest at the date the application is received or an earlier date if nominated (subject to availability of necessary scheme information).

As noted, the main purpose of this information is to enable a superannuation interest to be valued. For defined benefit schemes like SASS, SSS and PSS, this is a complex task. Currently, the fund itself will not actually provide a value for a benefit but rather, will provide information that enables others — generally the parties to the marriage or Family Court — to do so. This involves following rules set out in the Family Law legislation to select a valuation method and factors contained in tables within that legislation. These methods and factors, when combined with the information provided by the fund — eg. the salary and benefit multiple that the interest is based on — enable the current dollar value of the benefit to be determined, based on the specific valuation methods in the Family Law provisions.

If a fund believes that there is an alternative method of valuing its superannuation benefits that provides a more accurate result than may be achieved using the default Family Law approach, it may apply to the Commonwealth government for approval of the alternative valuation method. On the basis of actuarial advice which considers the default Family Law methods and factors to be inappropriate for the STC schemes, the NSW Premier's Department and the Scheme Trustee are applying for an alternative methodology to be used for the STC schemes. At the time of writing this article (October 2003), confirmation is awaited of whether or when the proposed alternative valuation methodology may be implemented for STC members seeking to have their benefit valued for Family Law purposes.

You should seek professional legal advice before acting on any information provided.

Flagging a superannuation interest

Benefit *flagging* is a key part of the Family Law rules as they apply to accruing superannuation interests during the contributory phase. The purpose of a flag is to alert a superannuation fund that it should not pay a benefit to a member without first telling the marriage partners and the Family Court that a benefit is about to be paid. This is to enable an agreement or Court Order to split the payment to be provided to the fund so that the benefit can be shared between the parties to a marriage which has broken down.

A flag is generally expected to be applied where a benefit payment is likely to occur reasonably soon and a decision has not yet been made on whether or how the benefit might be split. A benefit payment flag can be set by Court Order or by agreement between the marriage partners. Parties to a marriage could agree to a flag at any time, as long as they are separated or divorced.

A superannuation interest can only be flagged if the scheme member is either:

- not eligible to receive a benefit payment when the flagging notice is received, or
- is eligible, but has not yet applied for benefit payment.

A benefit that has already been paid or has begun to be paid to the member (eg. a pension) cannot be flagged.

In limited circumstances, payment of a certain benefit amount may be made even though a flag is in place. Examples of this include an amount released to a scheme member on compassionate or financial hardship grounds in accordance with the Commonwealth rules.

Splitting a superannuation interest

A superannuation interest may be split so that it can be shared between the parties to a marriage which has broken down. A split can be imposed by agreement between the parties or by Family Law Court Order. Under current legislation, the member's record in the scheme will be noted with details that the interest is subject to a payment split. A scheme member's superannuation benefit is reduced by an amount equivalent to the benefit share allocated to the non-member spouse. The split can only occur when the member applies for a benefit to be paid from the scheme, which can be some time in the future.

In the case of a Court Order, the Family Law legislation provides for the fund to be provided with a draft order in the first instance, so that it can check that the order can actually be implemented on an administrative and practical

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level and is in line with relevant legislation. This process is called *procedural fairness*.

A superannuation interest valued at less than \$5,000 cannot be split. In addition, certain benefit payments cannot be split, including payments made to the scheme member on financial hardship or compassionate grounds, as well as payments of insurance-type incapacity benefits and temporary incapacity benefits.

| Types of benefit split

An agreement between the parties or a Court Order will generally provide that a certain dollar amount must be allocated to the non-member spouse as that person's share of the interest. This is called the *base amount*. If the base amount cannot immediately be paid out of the fund, either directly to the non-member spouse or to another superannuation fund nominated by the non-member spouse, as is currently the case with the Pooled Fund — see ***When is a split benefit payable to a non-member spouse*** below — the base amount is adjusted for investment earnings or by some other method, until it does leave the fund.

An alternative method for splitting a superannuation interest is where an agreement or Court Order specifies a percentage split that will apply to actual benefit payments. An example could be where the Family Court Orders that 50% of any benefit payment must be allocated to the non-member spouse. In reality, a different percentage may apply depending on the circumstances of the couple and the range of property interests being split (eg. a house, car etc).

If a scheme member is currently receiving a pension, it would be more appropriate that the order specify a percentage split. That percentage would then apply to each pension payment made to the member.

The wishes of the parties may also determine how different interests, including superannuation, may be split, either by *base amount* or the percentage method, especially if the split is made by way of agreement between the parties.

A fee of \$88 (including GST) (\$44 each) is currently payable by the parties for splitting a superannuation interest and is deducted from the benefit of each spouse at the time of the split.

| When is a split benefit payable to the non-member spouse?

If an agreement or Order to split a superannuation interest is received by a fund, it does not mean that the amount allocated to the non-member spouse will be immediately split from the member's interest. Under the Family Law

legislation, the amount payable to the non-member spouse is to be paid when a splittable benefit ***becomes payable to the member***. What this means is that the non-member spouse will only receive their share of the superannuation interest when the member becomes entitled to and elects to receive a benefit following employment exit eg. on resignation, retrenchment, age or invalidity retirement.

A member who exits employment before becoming eligible for a retirement benefit has the option to defer their benefit in the scheme until a later date, which may be on or after reaching the scheme retirement age. In the case of benefit deferral, the superannuation interest of the non-member spouse becomes payable when the scheme member applies for benefit payment.

Before payment, the member's interest will be flagged with the split details. Both parties receive annual benefit statements which set out the current values of their respective entitlements.

Where a non-member spouse's benefit is paid from a scheme it can be paid direct to the beneficiary only where one of the standard Commonwealth *conditions of release* that apply to superannuation benefits generally, is satisfied by the non-member spouse. These conditions are explained in the annual benefit statements sent to members each year.

A non-member spouse will be advised of the payment rules when the benefit is initially split and in subsequent annual statements.

Where direct payment cannot immediately be made to a non-member spouse, the benefit must be rolled over to another superannuation fund nominated by them, for preservation until a condition of release is met.

| Possible legislation changes

It should be noted that the Family Law legislation does allow Trustees to put in place rules for the *immediate splitting* of interests. These rules allow the superannuation interest to be split when the splitting order or agreement is received rather than having to wait for the scheme member to be paid a benefit. However, the Pooled Fund's rules and legislation do not currently allow for immediate splitting rules to be put in place.

It is possible that changes to the STC scheme legislation will be introduced in the future to enable a non-member spouse's share to be paid immediately. Any such legislation will not change the payment/rollover rules explained immediately above. However, if introduced, it will give the non-member spouse earlier access to benefit payment where a condition of release is already satisfied. Alternatively, it will enable them to roll over their share of the benefit to a fund of their choice sooner than allowed for under the current arrangements.

Big improvement in the Pooled Fund's 12 months rolling return

At 30 June 2003 the 1 year net return for the Pooled Fund was a negative 1.7%. Three months later at 30 September, the 1 year net return was a positive 7.3%, which was made up of the following quarterly returns:

	Dec Quarter 2002 %	Mar Quarter 2003 %	June Quarter 2003 %	Sept Quarter 2003 %
Pooled Fund	2.6	-2.9	4.6	2.9

The rapid improvement in the 1 year rolling return is partly technical and partly a function of sentiment becoming positive about world growth, which in turn influences the outlook for earnings growth.

Last year, markets were very difficult during the September quarter 2002 and most super funds with a high allocation to growth assets did poorly. The Pooled Fund returned a negative 5.7% for that quarter, which was slightly below the negative 5.4% return generated by the median growth manager in the InTech* performance survey. However the return for the September quarter 2002 is no longer required to calculate the 12 months return. It has been replaced by the return for the September quarter 2003, which is a positive 2.9%. Not surprisingly, replacing a negative 5.7% with a positive 2.9% generates a major turnaround in the return figures. However, the real reason for the turnaround is the perceived improvement in the fundamentals underlying the various investment markets.

There has been a growing perception over the past 6 months that the effects of easy monetary policies combined with significant fiscal stimulus in the US would rekindle economic growth. Investors have shown confidence in this scenario by preferring growth to defensive assets. Reflecting this preference, in the 6 months to 30 September 2003, Australian shares returned 12.2% compared with Australian

bonds of 1.9%. (There is a split of a similar magnitude between unhedged international shares and bonds.)

Going forward there are a number of constraints, including minimal job creation, rising household debt and protectionism, each of which could undermine the present global economic outlook. However, investment markets are currently focusing on the improvements in economic activity rather than the potential problems.

Net investment returns for periods ending September 2003

	3 Months %	1 Year %	3 Years % per annum	5 Years % per annum
Pooled Fund	2.9	7.3	-1.1	4.6
Median Manager — InTech* Surveys	2.9	7.0	0.4	4.8
Growth				
Asset Sector Index Returns				
Australian Shares	5.9	11.4	2.5	8.0
International Shares (unhedged)	3.9	0.5	-16.7	-2.4
Listed Property Trusts	-4.2	6.2	11.3	8.5
Australian Fixed Interest	-0.2	5.5	7.3	5.8
International Fixed Interest (hedged)	0.0	6.5	9.0	6.7
Cash	1.2	4.9	5.1	5.2

Investment returns in the Pooled Fund are not guaranteed by the Trustees of the Fund or the NSW Government. Past performance is not an indication of future performance.

**InTech is an asset consulting firm which publishes surveys of the investment performance of superannuation fund managers.*

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