

WHAT SPECIES OF ASSET?

Binding financial agreements that deal only with superannuation

By MARK MACDIARMID

Uncertainty still exists around whether and how a superannuation interest is property and what effect its inclusion may have on a financial agreement.

Mark MacDiarmid is an Accredited Specialist in Family Law at Turner Freeman Lawyers.



THE QUESTION OF WHETHER OR not a superannuation interest was property for the purposes of the *Family Law Act 1975* (Cth) (the FLA) was a vexed issue prior to the introduction of Part VIII B of the Act.

Because a s.79 order adjusting the economic interests of parties to a marriage must be directed at “property”, any class of asset which falls outside the definition of property cannot be the subject of a s.79 order. Part VIII B clarified the issue, not by deeming superannuation to be property, but by extending the court’s jurisdiction to make orders with respect to

this “other species of asset”.

The common wisdom now is that following the full court of the Family Court’s decision in *Coghlan and Coghlan*,¹ it is unnecessary to consider whether or not a superannuation interest is property, since the court can deal with the interest under s.79 regardless of its true characterisation.

Nevertheless, an issue remains in the Part VIII A and Part VIII AB financial agreement provisions of the FLA, since if a purported financial agreement fails to deal with the property, financial resources or maintenance of the parties, it will not be a financial agreement for the purposes of the FLA, and will not succeed in displacing the court’s ability to adjust the parties’ interests under s.79 (for married couples) or s.90SM (the equivalent provision for de facto couples).²

If the only subject matter of a purported financial agreement is superannuation, and superannuation is not property or a financial resource but, in the words of the majority of the full court in *Coghlan*, “another species of asset”,³ the agreement will not be a “financial agreement” and cannot therefore be “binding”.

So what is the true characterisation of a superannuation interest? In particular, what is the status of that elusive comment in *Coghlan* that superannuation is another species of asset? Does the thinking behind that statement leave untouched the earlier case-law characterisation of superannuation as a financial resource, or has the conscious decision of the legislature to single superannuation out for special treatment made it

something that sits in its own puddle, just as income does?

In seeking to clarify their view that superannuation constitutes “another species of asset” (*Coghlan*), the full court made the following significant observation: “It is interesting to note in this regard that, from its inception, s.75(2) has contained reference in paragraph 75(2)(b) to ‘property and financial resources’ and then in paragraph 75(2)(f) has contained reference to ‘a ... benefit ... under any superannuation fund or scheme’. Thus, the treatment by the legislation of a superannuation benefit or entitlement as a concept separate from property and financial resources is not new.” [emphasis added].⁴

Is the full court suggesting here that superannuation has never been a financial resource, and those cases that have treated it as such are mistaken? On this argument, prior to the introduction of Part VIII A, the only appropriate place to examine superannuation was in an evaluation of s.75(2)(f).

Set against this is the court’s comment that even in the absence of a splitting or flagging order being sought, the court could still treat superannuation as property for the purposes of including it in the first step, if it were satisfied that that were its true characterisation.⁵ Given that the characterisation of superannuation may still be a live issue in the area of financial agreements, it should be noted that since the introduction of Part VIII B we have had the benefit of the High Court’s decision in *Kennon and Spry*,⁶ which case may hold the key to treating superannuation interests as property. ⇨

How was superannuation traditionally treated?

Prior to the introduction of Part VIII B, there was some inconsistency as to whether superannuation was to be treated as property or as a financial resource. Nevertheless, it is probably fair to say that the better view, expressed here by Nygh J, was that “a member has an interest in the fund which is protected by law to ensure that the fund is properly administered ... which is ‘property’”.⁷

However, in discussing the then recent High Court decision in *Official Receiver in Bankruptcy v Schultz* (1990) 64 ALJR 651, his Honour went on to speculate that the interest of the member is analogous to the interest of a beneficiary under a will before the estate is administered, and “such a beneficiary has no proprietary interest in the assets which make up the estate even though the assets may have been left to him or her under the will.”⁸ The right of the beneficiary is ‘a continuing right of uncertain ultimate worth. It remains a right belonging to each of the named beneficiaries, in relation to the whole of the estate and the management of the estate (at 655)’.⁹

At about the same time, the full court in *Harris and Harris*¹⁰ (Ellis, Strauss and Lindenmayer JJ) had said: “In our view, it can be said generally that an entitlement under a superannuation scheme is a chose in action and property to that extent.”

Nevertheless, in *Wunderwald and Wunderwald*,¹¹ Nicholson CJ, Strauss and Cohen JJ noted: “In a case where parties can clearly put themselves in a position of obtaining their entitlements to a superannuation fund, without suffering any detriment, such as the loss of the opportunity to continue with their career and in a case, such as this one, where the trustee of the superannuation fund is clearly the creature of the parties or one of them, it seems to us to be quite unreal to treat such an entitlement as other than property which is available for distribution pursuant to s.79. In such a case it seems to us that the distinction between ‘property’ and a ‘financial resource’ is a distinction without a difference.”¹²

But as the full court had already observed, this sort of case was in the minority (although it should be noted that this must now be a sizeable minority given the explosion in recent years of self-managed funds). The full court seemed to approve the general approach that regardless of the fact that an entitlement under a superannuation scheme was a chose in action and therefore property, this property was nevertheless *a continuing right of uncertain ultimate worth*, and it was generally preferable to treat that interest as a financial resource under s.75(2).

Coghlan

In 2001 the new Part VIII B introduced the following section into the FLA as s.90MC: “A superannuation interest is to be treated as property for the purposes of para (ca) of the definition of matrimonial cause in section 4.”

In *Coghlan*, the full court (Bryant CJ, Finn and Coleman JJ in the majority, Warnick and O’Ryan JJ dissenting) observed that “s.90MC does no more than operate to extend the definition of ‘matrimonial cause’ by extending the jurisdiction, which the various courts which exercise the jurisdiction under the Act have in proceedings between parties to a marriage with respect to their property, to include a jurisdiction to make orders with respect to the superannuation interests of the parties to property settlement proceedings.”¹³

In the view of the majority in *Coghlan*, a superannuation interest comprises a species of asset that is dealt with according to Part VIII B, and which may or may not also be property under s.4(1). But there is no need for the court to go to the extent of determining whether or not such an asset is also property under s.4(1), as its special treatment under the FLA means that the court is “relieved from having to determine”¹⁴ such a question.

While it is possible to read the majority’s view of s.90MS as prohibiting the interpretation that superannuation is ever to be treated as property,¹⁵ the statement in para 61 of the judgment that superannuation could be included in the first step, “where the court is satisfied that the superannuation interest is indeed property within the meaning of the definition of property contained in s.4(1)”, seems to indicate that the proper interpretation is that whether or not superannuation is property under s.4(1), if the superannuation interest comes within the definition of s.90MD it may be dealt with by the court.

The evil that the majority was addressing itself to was the erroneous idea that Part VIII B had the effect of *requiring* the court to view superannuation interests as synonymous with property.

The majority effectively said that whether or not a superannuation interest can be regarded as property is irrelevant, because in drafting Part VIII B the legislature took the approach that it would expand the jurisdiction of the court to make orders under s.79 in relation to superannuation interests as defined in s.90MD of the FLA (although *in accordance* with Part VIII B: see note 1 to s.90MS(1)), rather than adopting an alternative approach of simply declaring superannuation interests to be property under s.4(1).

FAMILY LAW ACT

90MH. Superannuation agreement to be included in financial agreement if about a marriage

- (1) A financial agreement under Part VIII A may include an agreement that deals with superannuation interests of either or both of the parties to the agreement as if those interests were property. It does not matter whether or not the superannuation interests are in existence at the time the agreement is made.
- (2) The part of the financial agreement that deals with superannuation interests is a superannuation agreement for the purposes of this Part. □

Binding financial agreements (BFAs)

While *Coghlan* may be said to have settled the issue in relation to applications under s.79, the same cannot be said in relation to financial agreements under Parts VIII A and VIII B of the FLA between parties to a marriage.

In order for a superannuation agreement to bind the trustee, it must be contained within a financial agreement, and so all of the strictures on enforceability of financial agreements apply to superannuation agreements. Significantly, if a purported financial agreement only deals with superannuation (that is, no other property and no spousal maintenance) and superannuation is not property, then it may not be a financial agreement. This is because whether or not the financial agreement is made under ss.90B(2) and 90C(2) or 90D(2), under all three sections, to be a financial agreement the agreement must deal with all or any of the property or financial resources of either or both of the spouse parties or “the maintenance of either of the spouse parties”.

But isn’t superannuation at the very least a “financial resource”? Consider again that passage in para 53 of *Coghlan*: “the treatment by the legislation of a superannuation benefit or entitlement as a concept separate from property and financial resources is not new”.¹⁶

The situation with *de facto* financial agreements under Part VIII AB is probably identical, notwithstanding the somewhat different basis of the jurisdictional power granted to the Commonwealth by the referring states.

What if the super interest under consideration actually were property? The full court seemed to accept that if a particular super interest were, in addition to being “another species of asset”, property for the purposes of the s.4(2) definition,

then it could be dealt with at step one of the preferred approach. Presumably, its mixed status could also be relied upon to carry a financial agreement over the line if there were a threshold issue under ss.90(B), (C) or (D).

Enter Kennon & Spry

In *Kennon v Spry*¹⁷ the High Court was asked, among other things, whether the bundle of interests a couple had under a discretionary family trust amounted to 'property' for the purposes of the FLA. The situation was complicated not just by several amendments to the trust deed that were found to have been able to be set aside under s.106B, but by the fact that the wife was not a beneficiary, but merely one of a class of beneficial objects who could, by an exercise of the husband-trustee's discretion, potentially be elevated to the status of beneficiary. In addition, at the relevant time in the life of the trust, the husband was incapable of being either a capital or income beneficiary; hence his argument that there was insufficient connection between the assets of the trust and the parties to the marriage for those assets to constitute 'property of the marriage'.

Nevertheless, the court found that the husband's power of appointment (even in the absence of a potential right to appoint capital or income to himself) "was able to be treated ... as a species of property".¹⁸ Thus there were several articulated links between the wife and the valuable assets of the trust:

- there were her equitable choses in action for consideration as a potential beneficiary, and due administration of the trust;
- there was a trustee who was a party to the marriage;
- there was the actual power in that trustee to potentially make a distribution in her favour (itself another species of property), regardless of the fact that she was not a beneficiary, but merely one of a class of beneficial objects of the trust; and lastly
- there was the real and substantial trust property.

It was the sum of these articulated links that attracted s.79.

Kennon and Spry was not concerned with Part VIIIIB, but the majority decision nevertheless had the effect of rendering Mrs Spry's otherwise "continuing right of uncertain ultimate worth"¹⁹ into something capable of much more certainty: "because the relevant power permitted appointment of the whole of the trust fund to the wife absolutely, the value of that property was the value of the assets of the trust."²⁰ Similarly, in the case of a superannuation interest, it is reasonable to suppose that the jurisdictional expansion comprised in Part VIIIIB has the potential effect of elevating what might previously have been a "con-

tinuing right of uncertain ultimate worth" into something capable not only of being valued according to principles established by the legislature, but of being dealt with either by a splitting or flagging order.

In effect, Part VIIIIB takes on the linkage role of the trustee power in *Kennon and Spry*. Because "part of the property of the parties to the marriage, within the meaning of the Act, was [Dr Spry's] power to appoint the whole of the property to his wife",²¹ the High Court was able to complete the link between Mrs Spry's equitable choses in action and the tangible assets of the family trust. The trustee

be property under s.4(1), the fact that it opens the way for valuations of superannuation interests to be made and then for those interests to change hands must surely have the effect of rendering such interests "property" for the purposes of s.4(1).

Practical consequences for BFAs

The current wisdom is that, in preparing a BFA, solicitors should ensure the agreement deals with more than superannuation alone, and nothing in this article should be regarded as urging anything to

"In many relationships, particularly where the parties have experienced insolvency, the only asset of any worth is superannuation."

power qua s.4(1) property (at least while it was in Dr Spry's hands, or subject to his control) was the vital link for the attraction of a s.79 order. Similarly, Part VIIIIB comprises a robust machinery for linking a party's interest in superannuation to the underlying assets of the superannuation trust by applying certainty of value to that interest, and exposing the interest to an order under s.79.

Once a splitting order has been made, then, depending on the superannuation trust deed, the spouse who has received the split interest could conceivably seek early access to the superannuation by reason of hardship. The potential availability of a splitting order (even if initially not sought) actually invests the superannuation interest with a quality of alienability which, though generally not considered to be necessary for an interest to be "property" under s.4(1),²² by being absent, triggered one of Heydon J's major objections to the wife's argument in *Kennon and Spry*.²³

Accordingly, even though Part VIIIIB immediately operates via a device that expands jurisdiction, rather than by declaring a superannuation interest to

the contrary. However, in many relationships, particularly where the parties have experienced insolvency, the only asset of any worth is superannuation. If a practitioner were to be presented with an already executed purported financial agreement which only dealt with superannuation, but which was in all other respects compliant with the stringent requirements of the FLA, the question of whether or not a superannuation interest is property could have serious ramifications for the enforceability of such an arrangement.

My own feeling is that if the matter were to be decided in court, it could be successfully argued that there is plenty of pre-Part VIIIIB authority for the proposition that superannuation is a financial resource, and that an appropriate interest might even be property, either because it is a self-managed fund (as in *Wunderwald*) or because, since *Kennon and Spry*, that must now be the natural conclusion to draw. And if such is the case, the appropriate subject matter for a financial agreement is covered.

But I don't necessarily want one of my clients to be the first to risk such an argument. □

ENDNOTES

1. (2005) FamCA 429.
2. See ss.90B(2) and 90C(2) or 90D(2) of the FLA.
3. *Ibid* at para 40.
4. *Ibid* at para 53.
5. *Ibid* at para 61.
6. [2008] HCA 56.
7. *Evans and Public Trustee of Western Australia* [1991] FamCA 16 at para 3 per Nygh J.
8. *Horton v Jones* (1935) 53 CLR 475 at 486.
9. [1991] FamCA 16 at para 4.
10. (1991) FLC 92-255 at 78,710.
11. (1992) FLC 92-315.
12. *Ibid* at para 23.
13. (2005) FamCA 429 at para 38.
14. *Ibid* at para 53.

15. "There is nothing in our view in s.90MS(1) which indicates that superannuation interests are to be treated as property in proceedings under s.79 (irrespective of whether or not an order under Part VIIIIB is sought in those proceedings)", at para 40.
16. *Ibid* at para 53.
17. [2008] HCA 56.
18. *Ibid* at para 79 per French CJ.
19. *Evans and Public Trustee of Western Australia* [1991] FamCA 16 at para 4 per Nygh J.
20. [2008] HCA 56 at para 137 per Gummow and Hayne JJ.
21. *Ibid* at para 126 per Gummow and Hayne JJ.
22. *Best and Best* (1993) FLC ¶92-418.
23. [2008] HCA 56 at para 162. □