12. Members' rights

Introduction

12.1. This chapter discusses a number of issues surrounding the relationship between superannuation schemes and their members. First, it deals with the extent to which members can exercise control over the activities of their schemes. This includes the ability of members to transfer their investment to another scheme and member representation on the board of the responsible entity. Secondly, it considers the rights that members have to enforce the fiduciary and other obligations that the responsible entity owes them. Thirdly, it examines a number of alternative means of resolving disputes between members and responsible entities. Fourthly, it considers the desirability of earlier vesting of contributions, the reduction of qualifying periods of service and of restricting relief in hardship cases. Finally, the chapter deals with the rights of scheme members to their superannuation entitlements on the bankruptcy of the scheme member or employer sponsor and on the divorce or separation of spouses or de facto spouses.

Consumer control of superannuation

Different types of schemes offer different means of control to members

12.2. Control over a superannuation scheme can be exercised by members in two ways. First, members may simply leave the scheme. This option is available to members of personal superannuation schemes. While it may not provide members with direct control concerning the activities of scheme management, it acts as a disciplinary mechanism on the responsible entity. Secondly, members may have input into the decision making process of the scheme. This happens in single employer sponsored and industry schemes because of the Commonwealth's policy of requiring member representation on the controlling bodies of superannuation schemes.

Consumer sovereignty and personal superannuation schemes

12.3. *Ability to transfer.* Economic theory postulates that the freedom of consumers to choose how they dispose of their income is vital to the efficient allocation of resources in a market economy. Consumers of personal superannuation schemes and ADFs generally have the right to switch their contributions from one scheme to another. The ability of members to 'vote with their feet' can be a significant control over scheme management, as it acts as a form of partial liquidation.[1] However, the transfer of contributions from one scheme to another can involve quite high transaction costs. This reduces the likelihood that this option will be exercised. As competition between offerors of such schemes increases, particularly if new offering institutions such as banks emerge, the transaction costs are likely to fall, making it easier for members of these schemes to express dissatisfaction with their scheme in this way.

12.4. *Schemes subject to the prescribed interests provisions of the Corporations Law.* Subject to the terms of the deed or other instrument constituting the scheme, members of schemes that are prescribed interests[2] have the rights and powers to control their schemes as set out in the Corporations Law.[3] These rights include the ability to enlist the aid of the Australian Securities Commission (ASC) in taking action against the promoters of a scheme.[4] However, as has been demonstrated by the recent turmoil in the property trust sector, these rights appear to be ineffective in enabling investors to exercise any significant influence over the direction of the policies of a scheme. The most practical means available to members to express dissatisfaction with such a superannuation scheme's performance is to transfer their funds to another scheme.

12.5. *Schemes subject to the Life Insurance Act.* Members of these schemes have neither the right to become directly involved in the management of their scheme nor the right to enlist the aid of the insurance industry regulator (the ISC) in the way members of prescribed interest schemes can enlist the aid of the ASC. They must rely on the vigilance of the ISC[5] or 'vote with their feet' and transfer their contributions to another scheme. Once again, exercising the second option may involve high transaction costs.

12.6. *Recommendation.* The Review considers that freedom of choice is an essential feature of personal superannuation schemes. DP 50 proposed that, in accordance with existing policy, benefits in personal superannuation schemes should continue to be fully transferable. This proposal received wide support.[6] It therefore recommends no changes to the current transferability arrangements

1. Fama and McJensen, 'Agency Problems and Residual Claims', (1983) 26 *Journal of Law and Economics*, 327-50.
2. As defined in the Corporations Law s 9.
3. Corporations Law s 1069; Corporations Regulations reg 7.12.05; see also s 1084.
4. eg, under the *Australian Securities Commission Act* (Cth) s 50. This power is predicated on the ASC initiating an investigation and forming the opinion that the action is in the public interest.
5. They may provide the ISC with information which causes it to launch an inquiry into the insurance company using its powers under the *Life Insurance Act 1945* (Cth).
6. S McNelis *Submission* February 1992; Women's Economic Think Tank, *Submission* February 1992; ASFA *Submission* March 1992; WJ Burke *Submission* February 1992.

for personal superannuation schemes. In accordance with existing policy, where superannuation schemes permit members to transfer their benefits to another scheme other than on termination of employment, benefits should continue to be fully transferable, subject to a redemption period appropriate to the assets of the scheme.

Recommendation 12.1: Personal superannuation funds: transferability restrictions

There should be no change to the law in relation to the ability of members of personal superannuation funds to transfer or withdraw their benefits.

Consumer sovereignty in employer related schemes

12.7. *Limited transferability.* When membership of a superannuation scheme is offered by an employer, it is generally a condition of the offer that the employee may only join the scheme nominated by the employer. In a few cases employers will offer employees the opportunity to nominate a personal scheme to which the employer agrees to make contributions on behalf of the employee. This option is not available to members of industry schemes, where the superannuation scheme is either identified in the relevant industrial award or agreed by each employer and union. While the introduction of the SGL will ensure that many more employees benefit from superannuation, it will not change these limited choices.

12.8. *Transferability in employer sponsored schemes — problems and difficulties.* The virtual absence of direct competition for members of employer related superannuation schemes has recently been the subject of public debate. It has been suggested by some that members of compulsory single employer sponsored schemes and industry schemes should be able to choose which scheme their employer's contribution is paid into, including contributions required to be paid under the SGL legislation.[7] The *Industrial Relations Act 1991* (NSW) provides that employers may agree to pay contributions into a scheme other than that nominated in the award.[8] There are, however, problems with this proposal. First, there is some risk that it may encourage members to focus on short term performance rather than on long term performance. Secondly, to the extent that members do exercise their right and transfer their benefits, these schemes will have to increase their liquid and realisable assets to meet the demand for repayments, which could lower the overall return on the scheme's investments,

7. eg, Hewson and Fischer *Fightback!* Supplementary paper No 2 'Superannuation', 21 November 1991, para 2.4.6.
8. s 180.

thus diminishing the ability of the scheme to provide significant additional retirement income to scheme members. Thirdly, these schemes would also be subject to the possibility of a 'run' by contributors in the wake of performance significantly below average. This is a risk these schemes do not presently face.[9] This is perhaps the most important consequence for single employer sponsored schemes. As single employer sponsored schemes are, in general, smaller than personal schemes, they could suffer significant damage from such a 'run'. Fourthly, as a result of the short term focus of members and increased liquidity of funds, these schemes may be much less likely to invest in long term projects, such as infrastructure development. This may increase political pressure to force all schemes to invest in such projects, possibly at sub-commercial rates. Fifthly, on a practical level, employers, particularly large employers, would face significant administrative costs if superannuation payments on behalf of their employees were directed to a wide variety of superannuation schemes rather than to a single scheme.[10] Employers offering defined benefit schemes would face particular administrative difficulties if some of their employees chose to switch from their employer's scheme to a personal accumulation scheme and then attempted to switch back to the employer's scheme.

12.9. *Proposal.* In DP 50 the Review proposed that the existing transferability arrangements for single employer sponsored and industry superannuation schemes remain unchanged, namely that the law should not prescribe any level of transferability for single employer sponsored and industry superannuation schemes. This aspect of these schemes should continue to be regulated by the deed or other instrument constituting the scheme. Submissions supported this proposal.[11] Some, however, preferred that members of all schemes be allowed to transfer to another scheme without penalty.[12] For the reasons discussed, the Review remains of the view that it is not appropriate to prescribe any level of transferability for single employer sponsored or industry schemes. Accordingly, it recommends that the law should not prescribe any level of transferability for industry and single employer sponsored superannuation schemes. Transferability in these schemes should continue to be regulated by the deed or other instrument constituting the scheme. If those schemes offer transferability, the Review recommends that the value of the benefit is to be calculated at the date

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9. See Ross, *Retirement Incomes: Communicating a Vision for the 21st Century*, speech to Conference of Major Superannuation Funds, Wollongong, March 1992, 3.
10. The Review notes that some employers now limit the bank accounts employees can have their salary deposited into on the basis that the administrative problems associated with allowing their employees complete freedom of choice are too great.
11. ASFA *Submission* March 1992; ACTU *Submission* March 1992; Jacques Martin Industry *Submission* February 1992; Shell Australia Limited *Submission* February 1992; IFA *Submission* February 1992; LIFA *Submission* March 1992.
12. eg ASC *Submission* March 1992.

when the employee has done all that is required by him or her for the sum to be calculated. Interest at a prescribed rate should be payable from that date until payment. An employee who does all he or she has to do to withdraw should not suffer the consequences of further changes in the value of the fund.

Recommendation 12.2: Single employer sponsored and industry schemes: transferability restrictions
1. There should be no change to the law in relation to the ability of members of employer related superannuation funds to transfer or withdraw their benefits: these should continue to be governed by the provisions of the deed or other instrument constituting the fund.

2. The law should provide that, despite any provision in the deed or other instrument constituting the fund, the date as at which the amount of a payment to which a member of an employer related superannuation fund is entitled on withdrawing from the fund otherwise than on ceasing the employment to which his or her membership relates is to be worked out is the date on which the member completes all that is required of him or her to withdraw from the fund. If payment is made after that date, interest, at a rate to be prescribed, should be payable on the amount outstanding.

Member representation — an alternative means of member control

Introduction

12.10. Recent federal Government announcements about superannuation have stressed the importance of the accountability of responsible entities to scheme members.[13] For members of schemes out of which members cannot transfer their benefits other than by leaving their current job or industry (that is, employer related schemes), member representation on their scheme's responsible entity is an important part of improving that accountability. It is also an important element of the supervisory framework for superannuation.

Employer related schemes

12.11. *Member involvement.* Members of complying single employer sponsored and industry schemes are able to influence their scheme through the member representatives on the board of management of the responsible entity.[14] An

13. Treasurer's statement, paper 1 para 6.
14. The members also have all the power that the beneficiaries of a trust have.

equal number of employer and member representatives are required for the boards of large (that is, those with 200 or more members) industry and single employer sponsored schemes.[15] Employee representation is optional for smaller funds.[16] Having members on the boards of responsible entities of these schemes provides an active role for members in the management and protection of their money, particularly where the member representative is in constant contact with the other members of the scheme.[17] They can provide direct member feedback to the responsible entity.

12.12. ***The Review's proposal.*** The Review is of the opinion that it is desirable gradually to make equal representation for smaller schemes (that is, less than 200 members) compulsory, instead of optional as at present. The Review recognises that, where the members of a scheme are also the principals of the employing enterprise, there is no need for such requirement, as the employees and their employer have no conflicting interests. In principle, it would seem desirable to extend the requirement for equal representation to all schemes with members who are not also principals, that is, arms length members. The Review recognises, however, that such a recommendation may not be practical. In DP 50 the Review proposed that equal representation of members and employers on responsible entities of single employer sponsored and industry schemes should be extended by 1998 to all schemes with five or more members.

12.13. ***Submissions.*** Submissions showed considerable support for extending equal representation beyond schemes with 200 or more members. Exactly where the cut off point should be was not clear.

> Equal representation is a cornerstone of ASFA's preferred model of prudential control based on active member interest and involvement. Conceptually, therefore, we would support an extension of the equal trusteeship requirement wherever there are arms length members. We are, however, concerned about the costs of equal trusteeship which can be considerable (on a per member basis) for smaller funds.[18]

15. OSS Regulations reg 13.
16. OSS Regulations reg 15.
17. Member representatives are obliged to act in the interests of all members of the scheme, not just in the interests of the members who elected them or on whose behalf they were appointed.
18. ASFA *Submission* March 1992.

Some submissions suggested a threshold of 10,[19] others 50.[20] Concern was also expressed that, apart from cost, the number of members in smaller schemes who would be prepared to be trustees may not be sufficient.[21] One submission expressed the view that equal representation does not go far enough.

> Whilst it is acknowledged that employers have initiated many of the superannuation schemes, that should be no reason for the employer to have equal status on the responsible entity. In light of the very fact that the employers have often initiated the establishment of a superannuation scheme, there should be a positive and absolute requirement that the employee members of the scheme should have the majority representation on the responsible entity. This would ensure that there cannot be a circumstance in which the will of the employee members of the scheme can be thwarted by the employer representatives on the scheme.[22]

12.14. ***Independence of the responsible entity.*** The Review has considered whether, even with member representation, responsible entities are sufficiently independent of the underlying contract of employment between the employer and the employee members of the responsible entity to be able always to act in the best interests of members. The governing rules of schemes with 200 or more members may, with the written approval of the ISC, appoint an independent body corporate as the sole trustee of the scheme. The members and the employer of a scheme with fewer than 200 members may agree to appoint an independent body corporate as trustee.[23] The Review considered requiring an independent chairperson for the responsible entity, either with a power of veto or with no voting power. Neither of those options seemed appropriate or feasible as a mandatory requirement.[24] The Review remains concerned that employees should not be put in the position where, as trustees, they can be subject to undue influence from their employer. The most appropriate way to ensure that employers do not exert pressure on member representatives of responsible entities to act as the employer wants, even if that is not in the interest of the members of the scheme, is to make it an offence for an employer to dismiss, threaten to dismiss, intimidate or attempt to influence an employee for any reason connected to the actions of the employee as a member of responsible entity. There

19. Prudential Assurance Company Limited *Submission* February 1992; Pelham Webb and Co. *Submission* February 1992; D Knox *Submission* February 1992.
20. National Mutual *Submission* February 1992.
21. ASFA *Submission* March 1992.
22. J Ryan *Submission* February 1992.
23. OSS Regulations reg 13(1)(e)(ii), 15(1)(a)(ii). The Review is of the opinion that the members of large schemes should also be able to have input into whether their scheme has an independent trustee.
24. There may not be enough independent chairpersons to go round.

are precedents for this type of offence.[25] Education of the members representatives as to their duties and obligations will increase their awareness of their obligations including their obligation to act solely in the best interests of the members of the scheme, as will the inclusion of such an obligation in the legislation setting out the fundamental duties of members of responsible entity boards.[26]

12.15. ***Employer representation.*** In DP 50 the Review raised for comment the issue whether the representation of employers on the boards of accumulation schemes should be phased out in the future.[27] Submissions that commented on this issue were generally of the view that employer representation on accumulation schemes should continue.[28] The Review does not propose to make any recommendation on this issue.

12.16. ***Recommendation.*** The Review has concluded that it is important to extend member representation to schemes below the current limit. It sees no point, however, in imposing on schemes a requirement that they may find impossible to comply with. Accordingly, it recommends that equal representation be extended to all schemes with 50 or more members. This requirement should come into operation in 1998 to allow time for members of schemes with between 50 and 200 members to arrange for appropriate training, if necessary.

Recommendation 12.3: Outlawing victimisation

The law should make provision similar to the *Industrial Relations Act 1988* (Cth) s 301 protecting persons who are members of the board of management of a responsible entity for a superannuation fund by making it an offence to threaten, coerce or intimidate, or prejudice in connection with their employment or otherwise, such a person on account of the exercise by the person in good faith of a power or duty as member of the board of management.

25. eg the *Human Rights and Equal Opportunity Commission Act 1986* (Cth) s 26 makes it an offence to dismiss, or threaten to dismiss, a person because he or she has made a complaint to the Commission.
26. See ch 9.
27. DP 50 para 9.8. The Review acknowledges that employer representation on the board of a defined benefit scheme is clearly appropriate as it is the employer who bears the risk of the scheme.
28. eg Western Mining Corporation Holdings Ltd *Submission* February 1992; LIFA *Submission* March 1992.

Recommendation 12.4: Employee representation

The law should provide that the conditions under which an employer related superannuation fund that has 50 or more members attracts a tax concession include a condition that the deed or other instrument constituting the fund makes appropriate provision to ensure that

- **the responsible entity for the fund not be an individual and**
- **the board of management of the responsible entity for the fund have at least one half of its members appointed (whether by election or otherwise) by the members of the fund.**

This provision should take effect from 1998.

Members' rights and powers

Members' rights against the responsible entity

12.17. ***What rights members have and how they can enforce them.*** The Review has recommended that the fiduciary obligations owed by the responsible entity to the members of the scheme be clarified.[29] Subject to what is said below about alternative dispute resolution mechanisms,[30] the main way of enforcing these obligations will be through legal action. Remedies available include injunctions to prevent or halt a breach, and, in some cases, recovery of compensation for loss or damage caused by a breach.[31] The enhanced representative procedure now available in the Federal Court may further assist civil action by members.[32] In appropriate cases, the responsible entity's dealers licence, if it has one, can be revoked by the ASC in the exercise of its existing powers.

12.18. ***Removing the responsible entity.*** In DP 50 the Review suggested that member representation, and the prospect of legal action by members of a single employer sponsored or industry scheme is not enough to ensure adequate member control of the scheme. The ultimate expression of member control is the ability to remove the responsible entity or, to be more precise, some or all the members of the board of the responsible entity.[33] The Review concluded, however, that this right should be restricted in the case of members of defined

29. See ch 9.
30. See para 12.30-12.42.
31. The Review recommends that the regulator should have injunctive powers and the power to take civil proceedings on behalf of a member to recover damages for loss suffered: see recommendations 13.7 and 13.11.
32. *Federal Court of Australia Act 1976* Part IVA.
33. If the members of a scheme agree to the appointment of a professional responsible entity the power discussed in this paragraph should be taken to mean the power to dismiss the professional responsible entity.

benefit schemes.[34] The Review proposed that a responsible entity (or one or more members of its board) should be subject to dismissal by a 75% majority vote of members who represent at least 25% of the total membership. Voting by postal ballot should be required except in the case of schemes where all members have the opportunity to attend in person. It was considered that high standards are appropriate for such an important decision. The proposal provided for a ballot to be requisitioned by 10%, or 50 of the members, whichever is less. The scheme should bear the cost of the ballot.[35] The proposal was intended to apply only to member representatives or members who had been appointed to the responsible entity by agreement between the members and the employer. Accordingly, it did not apply to personal schemes.

12.19. ***Response.*** The proposal was criticised in several submissions as being inconsistent with the general premise of trust law whereby the trustees act for all members of the scheme and should not, therefore, be subject to removal by '20% of the total fund membership'.[36] Some regard the opportunity at each election for members to remove the trustees who represent them as sufficient involvement for the members. ASFA opposed the proposal as it relates to the dismissal of the entire responsible entity. It considers that such an approach is likely to draw industrial issues and disputes into the trusteeship arena. It regards the dismissal of individual member representatives as workable but suggested that a particular representative should be subject to dismissal by a vote of his or her constituency. With regard to dismissal of the whole responsible entity, ASFA would prefer members to approach the regulator for the appointment of a judicial manager if they are dissatisfied with the performance of the responsible entity.[37] Strong support for the proposal was received from a number of individuals who made submissions.

> I agree wholeheartedly with the sentiments of the Discussion Paper which suggests that increased control should be able to be exercised by employees in relation to control over the responsible entity.[38]

The ASC supported the ability of members to remove the responsible entity subject to the modification that the vote required is 75% by value (not number) of members voting at a meeting of at least 25% (by value) of members.[39]

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34. This is because the investment risk does not lie with the members in those schemes but with the employer. The members alone should not, therefore, be able to dismiss the entire board of a responsible entity of such a scheme.
35. For defined benefit schemes, the employer will, in effect, bear the cost of such ballot.
36. eg Mercer Campbell Cook and Knight *Submission* February 1992.
37. As was suggested in DP 50 proposal 8.8. ASFA *Submission* March 1992.
38. J Ryan *Submission* February 1992.
39. ASC *Submission* March 1992.

12.20. ***Recommendation.*** If members are unhappy with the performance of an individual member who is a trustee or director of the responsible entity, they should wait until the next election, or appointment period, to remove that member. Alternatively, they could seek to have the regulator remove them from office. This would require the regulator to hold the opinion either that the person ought to be removed having regard to the risk he or she poses of non-compliance with the law or that the person is unable to fulfil his or her duties.[40] If members are dissatisfied with the performance of the responsible entity as a whole, they have the option of approaching the court for dismissal of the responsible entity and the appointment of a temporary responsible entity on terms and conditions as the court sees fit. The ground for such dismissal is that the responsible entity is unable to fulfil, or has failed to fulfil its obligations. Approaching the court would be an expensive exercise, possibly beyond the means of most members. They could seek the assistance of the regulator in taking the matter before the court.[41] The Review is not satisfied, however, that those options give the members adequate avenues of redress. Accordingly, it recommends that 10% of members of an employer related superannuation scheme should be able to call for a ballot for the dismissal of the responsible entity and to appoint an independent responsible entity to act for the balance of the responsible entity's term. This remedy should be available to members of defined benefits schemes as well as to those of accumulation schemes. Because at least two thirds of the members of a board of a responsible entity must agree to decisions of the responsible entity, it is reasonable that the entire entity be accountable to members. A 75% majority vote of members who represent at least 25% of the total membership of the scheme should be required to pass the resolution. The Review does not agree with the ASC that voting by value rather than by numbers is appropriate for superannuation schemes. Superannuation is a long term investment, and each member has a continuing interest in the success of the scheme. For the purposes of voting, 'members' should include all contributing members and adult beneficiaries. Voting should be by postal ballot unless the scheme is such that all members have the opportunity to attend in person. The vote should be by secret ballot in any case. The Review also recommends that the responsible entity be obliged to ensure that any notice it sends out convening a meeting of members contains adequate notice of any matters of which it is aware that are to be considered at the meeting, any resolutions of which it is aware that are to be put at the meeting and a summary of

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40. See recommendation 13.12.
41. See recommendation 13.8.

information relating to these matters and resolutions that is relevant to the decision of a member on how to vote at the meeting.[42] The notice would have to include the proposed replacement for the position of responsible entity.[43]

Recommendation 12.5: Members' power to replace responsible entity
The law should provide that the responsible entity for a superannuation scheme may be replaced as follows:

- **10% or more of the members of the fund, may, by notice in writing given to the responsible entity, require a ballot to be held for the removal of the responsible entity and the appointment of another person as responsible entity; the other person must consent to appointment as the responsible entity and give the declaration required by recommendation 8.7**
- **the responsible entity must then arrange for a postal ballot to be held on the question; if all members of the fund will have a reasonable opportunity to attend a meeting at which the question can be put, the responsible entity may arrange for such a meeting instead**
- **the responsible entity must, if it arranges such a meeting, also include in the notice of meeting a statement of the procedure to be put to the meeting as the procedure to be adopted by the meeting for conducting the meeting and for taking votes**
- **the question is not to be taken as having been agreed to unless at least 25% of the members cast a vote and the votes in favour of it amount to at least 75% of the members voting.**

The law should provide that this provision does not prevent other business being transacted at the meeting.

Mergers of superannuation schemes

12.21. ***Proposal.*** The development of the superannuation industry may well result in rationalisation through mergers. The merger mechanism for the joining together of two schemes is usually a matter for each deed. In many cases, however, schemes have incompatible merger provisions. In DP 50 the Review

42. These matters are required by one of the prescribed covenants to bind certain parties in a prescribed interest scheme. Corporations Regulations reg 7.12.15(1)(g).
43. The Review considered whether the regulations should prescribe who may be appointed as independent responsible entity in this case. It anticipates that professional trustee companies would be selected in most cases and does not propose prescribing this.

proposed that the regulator should have the power to propose a merger of two or more schemes to the members of those schemes. It also proposed that the regulator should develop guidelines for merger provisions in superannuation schemes.[44]

12.22. ***Submissions.*** The proposals received reasonable support.[45] A number of submissions expressed reservations, however. Some were concerned to ensure that the regulator could not force a merger, particularly of single employer sponsored schemes to take place.[46] Others saw no role for the regulator in this area.[47] The Review did not intend that the regulator should have power to force a merger against the wishes of the responsible entity or the members; rather that it should play a somewhat more pro-active role than it does at present in suggesting mergers where appropriate and where the responsible entities of the particular schemes may not have considered that as an option.

12.23. ***Recommendation.*** The Review has concluded that the option of merging is important and should be available to all schemes. Accordingly, it recommends that provisions in trust deeds that prohibit or limit a merger should be invalid. The decision whether to merge should rest primarily with the relevant responsible entities. The regulator should, however, be advised of a proposed merger.[48] The members of both schemes should also be advised of the proposal. If 10% of the members of either scheme request, in writing, a ballot on the proposed merger, a vote must be taken. The cost of that ballot is to be borne by the schemes. For the purposes of voting, members should include all contributing members and adult beneficiaries. If 75% of the members voting, representing at least 25% of the members of either scheme, vote against the merger proposal it is not to proceed. This right ensures that members retain power over their scheme.

Recommendation 12.6: Mergers

1. The law should provide that the conditions under which a superannuation fund attracts a tax concession include a condition that the deed or other instrument constituting the fund not prevent or restrict a merger of the fund with another fund, restrictions implied by the responsible entity's fiduciary obligations to the members of the fund apart.

44. DP 50 proposals 8.6, 8.7.
45. eg Jacques Martin Industry *Submission* 1992; ASC *Submission* March 1992; IFA *Submission* February 1992.
46. eg LIFA *Submission* March 1992; Department of Finance (Cth) *Submission* February 1992.
47. eg Prudential Assurance Company Limited *Submission* February 1992.
48. See recommendation 13.18.

2. The law should provide that the responsible entity of a superannuation fund must not put into effect a merger of the fund with another superannuation fund unless the entity has given written notice of the proposed merger

- **to the regulator and**
- **to the members of the fund.**

The period of notice is to be not less than 3 months. Failure to comply should be an offence.

3. The law should provide that, if 10% or more of the members of either fund, by notice in writing given to the responsible entity before the end of the 3 months, require a ballot to be held on the motion that the merger not proceed

- **the responsible entities must then arrange for a postal ballot to be held on the question; if all members of a fund will have a reasonable opportunity to attend a meeting at which the question can be put, the responsible entity may arrange for such a meeting instead**
- **the responsible entity must, if it arranges such a meeting, also include in the notice of meeting a statement of the procedure to be put to the meeting as the procedure to be adopted by the meeting for conducting the meeting and for taking votes**
- **the question is to be taken as having been agreed to by the members, unless at least 25% of the members of a fund cast a vote and the votes against the merger amount to at least 75% of the members voting in a scheme in which 25% of the members cast a vote.**

The law should provide that this provision does not prevent other business being transacted at the meeting.

4. If the motion is passed, the merger is not to proceed.

Members' rights over the policy of the scheme

Proposal to give directions

12.24. DP 50 suggested that the ways in which the members can control the operations of employer related schemes should not be limited to removing the responsible entity. It proposed that if enough members of a scheme agree on a particular course of action, they should be able to give binding directions to the responsible entity. A general meeting of members, or a postal referendum, should be able to be requisitioned by 10%, or 50, of the members, whichever is less. Such a meeting or referendum should be able to give directions to the responsible entity in relation to any matter affecting the scheme generally by resolution carried by a 75% majority vote of members representing at least 25% of the total membership. Postal and proxy voting should be permitted.[49]

Submissions

12.25. This proposal received considerable support although there was significant disagreement as to what should be the threshold for calling such a meeting[50] and the voting requirements. The proposal was rejected by some on the basis that the concept of members giving directions to a trustee to act in a certain way is inconsistent with trust law.[51] Concern was expressed about who would bear responsibility for action taken by a responsible entity pursuant to a direction by the members. The Review now considers that the right to give directions to the responsible entity may be open to abuse and could become a forum for playing out union disputes. Issues put to a meeting may involve a decision to put the interests of one group of members ahead of the interests of another group. The recommended external disputes mechanism[52] will improve the situation for members who have problems in relation to their own interest in the scheme. Those sorts of issues should never become an issue involving the entire scheme membership. As far as general policies of the scheme are concerned, the Review has concluded that election or appointment of member representatives should be the means by which they can be influenced. Where the members are strongly dissatisfied with the policies and performance of the responsible entity, mechanisms for the dismissal of the responsible entity are recommended.[53] Accordingly, the Review does not recommend that members should be able to give directions to the responsible entity. Without the power to direct responsible entities, the Review does not consider that an ability to call a meeting of members is of benefit to members and does not make any recommendation in that regard.[54]

Members' rights against external investment managers

12.26. As discussed in chapter 8, it appears that hired investment managers may owe fiduciary duties to members.[55] In DP 50 the Review suggested that

49. DP 50 proposal 9.5.
50. eg ACTU *Submission* March 1992; Office of Queensland Cabinet *Submission* February 1992; Jacques Martin Industry *Submission* February 1992; Department of Finance (Cth) *Submission* February 1992.
51. Department of Finance (Cth) *Submission* February 1992.
52. See recommendation 12.9.
53. See recommendations 12.5 and 13.12.
54. cf ASFA. It supported the requirement that members be able to requisition a general meeting but opposed the suggestion that such a meeting could give directions to the responsible entity.
55. See para 8.38.

managers should be subject to dismissal by the members.[56] The Review no longer takes that view. The duties owed by an external hired investment manager are primarily of a contractual nature and will be owed to the responsible entity. The members should have no right to remove an investment manager themselves. Usually, if a hired investment manager breaches its contractual duty to the responsible entity, the responsible entity will take action. Its own fiduciary obligations would require it to. If, for whatever reason, the responsible entity does not act, the regulator will be able to take legal action directly against the manager.[57] If the responsible entity fails to act against an investment manager that has breached its fiduciary obligations, and loss is suffered, the responsible entity will be liable to members for that loss. It can be argued though that the benefit of the fiduciary duties owed by a manager to the responsible entity are held on trust for the members.[58] Accordingly, the members could be said to have a right to join as a co-defendant an investment manager hired by the responsible entity of their superannuation scheme in any action against the responsible entity for failing to take action on a breach of fiduciary duty by the investment manager.

Advice and internal dispute resolution

Introduction

12.27. As superannuation coverage spreads throughout the workforce, more and more people will be dealing with superannuation schemes for the first time. The complexity of these schemes makes it more than likely that disputes will arise between responsible entities and their members. These disputes could range from not being able to gain access to the trust deed to a disagreement with the responsible entity's assessment of an application for benefits by a member on the basis that the member has been totally and permanently disabled. The following paragraphs look at the members' need for advice when a dispute arises, the current mechanisms for dealing with disputes, whether it is appropriate that disputes be dealt with other than by the responsible entity and possible alternatives.

An advisory service

12.28. ***Advice service covering all schemes.*** Education and information will play important roles in the success of individual superannuation schemes and, ultimately, the success of any retirement incomes policy. DP 50 therefore pro-

56. DP 50 para 9.14.
57. See recommendation 13.13.
58. See para 8.38.

posed that there be an easily accessible information and advisory service that covers all superannuation schemes, ADFs and DAs. The service would provide information and advice on issues such as members' rights, portability of superannuation benefits, unclaimed benefits, the interaction between superannuation and social security entitlements, dispute resolution, basic tax information and rollover options. DP 50 noted that one benefit of providing such information is that it would prevent many members' problems developing into fully-fledged disputes. It also noted that ASFA was considering establishing such a service for its own member schemes, and suggested that ASFA might be an appropriate body to administer the proposed service.[59]

12.29. ***Discussion and recommendation.*** The majority of submissions generally supported the proposal, but a number were concerned about practical issues such as funding.[60] ASFA has now indicated that it has abandoned plans to establish an advisory service, chiefly on grounds of coverage and cost.[61] In any event, most submissions supporting the proposal considered that the regulator should handle the advisory service.[62] In the light of ASFA's decision and of the consultations and submissions, the Review considers that it would be more appropriate for the regulator to establish and administer the proposed service. Furthermore, the service should not provide investment advice to retirees or anyone else. Later paragraphs discuss the desirability of schemes establishing internal dispute resolution mechanisms. The Superannuation Advisory Service should assist schemes to establish and use these mechanisms by setting up a panel of conciliators able to assist schemes on request. These conciliators would be particularly useful for smaller schemes. Questions of cost recovery also arise. There are strong arguments for such a service to be free to members, given the importance of superannuation to the Commonwealth's retirement incomes policy. Nevertheless, the Review considers that whether members are charged directly for the provision of advice, or schemes are charged directly for the use of the services of conciliators, or whether the members have to pay indirectly through levies on their superannuation schemes, is a question better left to government.

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59. DP 50 proposal 9.6.
60. eg Permanent Trustee Company Limited *Submission* February 1992; Westpac Financial Services *Submission* February 1992; ASC *Submission* March 1992; D Knox *Submission* February 1992.
61. ASFA *Submission* March 1992; D Shirlow, 'The ASFA Proposal in relation to an alternative dispute resolution mechanism for the occupational superannuation movement' *Paper* (unpublished) 25 March 1992.
62. eg LIFA *Submission* March 1992; ACTU *Submission* March 1992; AMP Society *Submission* February 1992.

Recommendation 12.7: Superannuation Advisory Service
1. A Superannuation Advisory Service should be established with the function of providing education and information to members of superannuation schemes about the operation of schemes and their entitlements as members.

2. The Superannuation Advisory Service should establish a panel of conciliators, able to provide conciliation services to assist in resolving disputes between members of superannuation funds, ADFs and DAs and the responsible entities for, or providers of, the schemes.

Internal dispute resolution mechanisms

12.30. *DP 50 proposal.* An advisory service would help to avoid problems and also ensure that problems did not develop unnecessarily into disputes. Even if an advisory service is established, however, the possibility of problems and disputes cannot be completely prevented. It is important, that members be able to approach their scheme with confidence that any problem they may have will be dealt with efficiently and thoroughly. DP 50 therefore proposed that each scheme should establish an internal procedure for dealing with member disputes, which would be free to members.[63] The existence and method of operation of the procedure should be made known to members.

12.31. *Submissions.* Most submissions supported this proposal. ASFA regards internal review and dispute resolution as particularly important. A number of industry based groups supported it in preference to later proposals for external review of superannuation scheme decisions.[64] Other submissions pointed to the importance of maintaining, as well as internal dispute resolution mechanisms, access to external mechanisms[65] and drew attention to the importance of independent reviews.[66]

12.32. *Recommendation.* There is widespread agreement that each scheme have an internal dispute resolution mechanism. Given the recommendation that the Advisory Service have a conciliation function, and the recommendations that the Review Panel be able to review decisions, but only if there is an internal dispute resolution mechanism, if that mechanism has been used, there is no need to require, as a matter of law, each scheme to have such a mechanism. The functions should emphasise informal methods of dealing with complaints and

63. DP 50 proposal 9.7.
64. eg ASFA *Submission* March 1992; LIFA *Submission* March 1992.
65. eg Australian Shareholders' Association Ltd *Submission* February 1992.
66. eg H Baker *Submission* February 1992; B Abrahams *Submission* March 1992; J A Ziedars *Submission* February 1992; R Cogger *Submission* February 1992; A Group of Members *Submission* February 1992.

problems, many of which may relate to administrative matters. Conciliation should be available when there is a dispute over the exercise of powers in relation to the members. The mechanism should be free to members — to encourage its use and to resolve disputes as early as possible. It will also be necessary to ensure that members are aware, when they enter the scheme, of the existence of the mechanism and how it operates. The Review recommends that this information be included in the member booklet or prospectus for the scheme given to members and prospective members.

Recommendation 12.8: Internal dispute resolution

1. Responsible entities for superannuation funds and ADFs and providers of DAs should be strongly encouraged to maintain a fair, easily accessible internal dispute resolution mechanism that is free to members.

2. The law should provide that the responsible entity for a superannuation fund, or an ADF and the provider of a DA, must include in each prospectus, member booklet or offer document issued to members or prospective members the prescribed particulars of the internal dispute resolution mechanism, if any.

External dispute resolution mechanisms

The present position

12.33. There are three established dispute resolution mechanisms, apart from the courts, available to members of some superannuation schemes.

- *LIFA scheme.* For those superannuation schemes provided by a life insurance company, the dispute resolution mechanism established by LIFA is available.[67] This involves an approach, in the first instance, by

67. This scheme has been criticised on a number of grounds, including, for example, that it is not seen to be independent of the insurance industry, and that there are too many steps before review by the Complaints Review Committee: see, eg, R Drake, *Superannuation Inquiries, Complaints and Disputes*, paper to ASFA Conference, November 1991.

the member to LIFA. If this proves unsuccessful, the matter is sent to a Complaints Review Committee. The decision of this Committee is not binding on the member, although it is binding on the insurance company.[68]

- *Banking Ombudsman.* If the superannuation is provided through a subsidiary of a bank that is a party to the Banking Ombudsman scheme and that subsidiary has been specifically designated, the Banking Ombudsman has jurisdiction.[69] Again, this is a private scheme that is based on a contract between participating banks. It is very informal, requiring only a contact by the member with the Banking Ombudsman's office. The emphasis is on conciliating complaints, but the Ombudsman can make a determination which is binding on the bank but not the customer.

- *Industrial Relations Commission.* Members of public sector superannuation schemes may appeal to the Industrial Relations Commission (IRC) if their internal appeals are unsuccessful. Additionally, members of award based superannuation schemes may complain to the IRC if the dispute concerns an alleged breach of the award.

Other schemes do not have an external dispute resolution mechanism. The Commonwealth has acknowledged that this is a deficiency in the coverage of the available alternative dispute resolution mechanisms. Further, the Commonwealth has indicated it believes there should be a suitable low cost dispute resolution mechanism to raise consumers' confidence in the superannuation industry and increase their willingness to invest in superannuation.[70]

DP 50 proposal

12.34. DP 50 examined a number of alternative options for external dispute resolution mechanisms. One suggestion was that a single dispute resolution mechanism be established for all superannuation schemes, a 'superannuation Ombudsman'. A detailed statement of the proposed Ombudsman's jurisdiction was suggested, including the following

68. ie, the insurance company's contract under which it participates in the scheme includes a provision that it will not contest an adverse decision by the Committee. If a company decided to breach this undertaking and ignore a decision of the Committee it is doubtful if the company's customer could enforce adherence to the contract (and hence the decision) as customers are not parties to the contract.
69. To date, there has been no such designation: Banking Industry Ombudsman *Submission* April 1992.
70. Treasurer's statement, paper 1 para 7.

- Issues affecting the scheme as a whole, such as the scheme's investment policy and strategy, reserving policy (if any) and selection of investment managers should clearly be outside the scope of the Ombudsman's jurisdiction.

- The Ombudsman should not have jurisdiction in disputes that are essentially industrial disputes, that is, disputes between members and their employers.

Submissions

12.35. Submissions from, and consultations with, industry groups showed considerable concern on this issue.

> AMP believes that an external dispute resolution mechanism is essential and that it would be better to establish it either under the direction of the regulator or an industry body such as ASFA. AMP does not believe that an Ombudsman would be satisfactory given the specialised nature of superannuation and the wide variety of superannuation arrangements in existence.
>
> Care will need to be taken regarding the nature of disputes which are able to be decided by this mechanism. [the proposal refers to] the jurisdiction of an Ombudsman over matters of fact such as qualification for total and permanent disablement benefits. Given that these benefits are generally provided under an insurance arrangement and the establishment and interpretation of the facts may be contentious, we would strongly dispute that this example should fall within the jurisdiction of a superannuation dispute mechanism.[71]

The Review's attention was also drawn to the need, in considering questions such as the degree of disablement, for responsible entities to consider and interpret medical evidence, often conflicting, and the overriding obligations of responsible entities to act in the best interests of the members. Other submissions expressed concern at the possibility of excessive use of such a scheme by frivolous complainants.[72]

The issues

12.36. ***Should there be external review?*** Under the present arrangements, a member of any superannuation scheme dissatisfied with a decision concerning him or her by the responsible entity can seek judicial review of the decision by the Supreme Court of the relevant State or Territory. For most people, this is

71. AMP Society *Submission* February 1992.
72. QUF Industries Ltd *Submission* February 1992.

simply an unrealistic option because of the cost involved.[73] It amounts to no right of review at all. The availability of review outside the court system depends on who is the responsible entity and whether the scheme is an industry scheme or one promoted by a life insurance company. Like treatment of like cases is a key indicator of justice. The federal Government has indicated its view that the differences in review rights, and the fact that members of some schemes have no access to review at all, is unjust and unfair. The Review has concluded that there should be a single mechanism available to members of all schemes with jurisdiction to review responsible entities' decisions affecting individual members.[74] The nature and scope of that mechanism are discussed in the following paragraphs.

12.37. *Who should be the review body?* A number of commentators on DP 50 criticised the proposal that there be an 'Ombudsman', preferring instead a 'panel'. The concern seemed to be that a single person — an Ombudsman — would not be as effective or efficient as a panel of persons. The Review agrees that it would be better if a panel of persons were to make up the review body. It should be independent of government, of schemes and the regulator. Because its function is to ensure fairness in schemes that help implement Commonwealth policy, its funding and resources should be provided from the Commonwealth. The need for the review to be independent was emphasised in several submissions.[75] To meet these requirements, the Review recommends that the panel should be appointed by the Minister from nominations by relevant interest groups. These would include consumer and union representatives, and representatives of suppliers of insurance products. It is important that at least some members of the review panel have experience and expertise in superannuation matters.

12.38. ***Kinds of decisions — the role of discretion.*** A not untypical clause in a deed establishing a scheme is

> Total but Temporary Disablement in relation to that Member shall mean the disablement of that Member resulting from an illness accident or injury (but excluding self-injury) which commences or occurs prior to the sixtieth (60th) birthday of the Member and as a result of which the Member has been continuously absent from employment for a period of at least three (3) consecutive

73. See ALRC 46 para 15-20.
74. Not all members of the Advisory Committee agree with this conclusion.
75. eg B Abrahams *Submission* February 1992; J Ziedars *Submission* February 1992; R Cogger *Submission* February 1992.

> months ending not later than the sixtieth (60th) birthday and in the opinion of the Trustee after consideration of such medical or other evidence as the Trustee may require the Member is unable to resume work in the Member's former occupation.

The Commonwealth Superannuation Scheme provides that

> **"[T]otally and permanently incapacitated"** means that, because of a physical or mental condition the person is unlikely ever to work again in a job for which he or she is reasonably qualified by education, training or experience or could be so qualified after retraining.[76]

In consultations it became clear that provisions of this kind are generally understood to give the responsible entity a discretion. The fact that a judgment has to be made whether a person is totally and permanently disabled, often on the basis of medical evidence, reinforces this view. As one commentator put it in discussions with the Review:

> [T]he majority of ill-health and total and permanent disability retirement claims involve the responsible entity in exercising its discretion to decide upon the eligibility of the claim. In these cases, there is little or no measurable physiological disability. Rather, they involve described but not physically detectable or measurable pain, constraint on movement, or, most difficult, psychological symptoms. These cases cannot be determined as matters of fact in the way that, for example, cancer, heart disease, or permanent organ or limb damage can... [A] judgement about them must be made by somebody on the basis of appropriate available evidence and that judgement takes on the character of fact.

12.39. ***Legal analysis.*** The responsible entity's obligation is to apply the terms of the deed or other instrument constituting the fund in accordance with fiduciary and other legal obligations. In the examples mentioned above, this involves forming a judgment whether the person 'is unable to resume work' or 'is unlikely ever to work again'. In many cases it will be difficult to make this judgment. But it must be made only on the medical or other evidence about the individual available to the responsible entity. It would be wrong, and a breach of its fiduciary obligation to the member, for the responsible entity to take into account, in forming that judgment, the effect on the scheme or on other scheme members if the judgment is made that the member is unable to work. There are, however, circumstances where the responsible entity will have to exercise a different kind of discretion. Provisions in deeds and other constituting documents governing the proportions in which members' dependants will be paid, and whether they will be paid at all, usually allow the responsible entity to

76. *Superannuation Act 1990* (Cth) Sch 1.

decide this matter 'in its absolute discretion'. In these cases, the effect of the decision on the interests of the other members is a relevant consideration that the responsible entity must take into account. The distinction between the two kinds of decisions is clear. The drafting of particular deeds may, however, not make it immediately clear which kind of decision is involved in a particular case.

12.40. ***Review.*** The Review recommends that both kinds of decision should be reviewable by the Panel just recommended. They are both presently reviewable by the courts. It is essential that a cheaper form of review should be available. The Panel should not decide the issue on the merits, except in limited circumstances. Its powers should broadly equate with those of the court. The Panel should first consider whether the responsible entity properly applied the law or the terms of the deed or other instrument constituting the scheme. The question should be, was the power of the responsible entity exercised legally and properly, that is, did the responsible entity, in making the decision

- fail to take a relevant consideration or matter into account
- take an irrelevant consideration or matter into account
- act in bad faith or with malice.

If the decision was not improper in that sense, it should not be interfered with. If it was improper, however, the Panel should be able to

- refer the matter back to the responsible entity to reconsider the matter and make a fresh decision in accordance with directions given by the Panel
- vary the decision
- substitute for the decision its own decision.

It should be emphasised that what the Review envisages is not a merits review. The Panel would not reconsider the issue afresh. It would only make a different order where it was satisfied that the original discretion had not been properly exercised. The Review Panel should be under a statutory requirement that it is bound, in deciding whether to make an order of the latter two kinds, by the same fiduciary obligations towards all the scheme members as the responsible entity. While it is, in the Review's opinion, important to have decisions that may have a significant impact on a person's post retirement income open to review, focussing the review, in the first instance, on the lawfulness of the exercise of the power by the responsible entity, and allowing a wider range of relief if the power was wrongly exercised, strikes the appropriate balance.

12.41. ***Who should be bound?*** For a review by the Review Panel to be effective, the responsible entity whose decision is the subject of the review will have to be bound by it. For constitutional reasons, the Review Panel will not be able to make orders that are, of themselves, effective to determine rights and obligations.[77] The LIFA scheme and the Banking Ombudsman scheme both operate on a contractual basis. The various parties to the scheme[78] have entered into a contract under which they undertake to be bound by the decisions given under the scheme. The clients (policy holders, members or bank customers) are not parties to these contracts. It is doubtful whether, because of the doctrine of privity of contract, they could enforce the contract. To ensure that superannuation responsible entities are bound, therefore, their access to tax concessions should depend on their complying with any order lawfully made by the Review Panel. The Review considers that a member who wants to use the Review Panel process should also be bound by the result, to the extent of waiving his or her right to take proceedings in a Supreme Court on the question. The decisions and actions of the Panel, however, should be open to judicial review under the *Administrative Decisions (Judicial Review) Act 1975* (Cth).[79] This will have the effect of ensuring that disputes can be quickly and cheaply disposed of, while preserving the right to approach a court.

12.42. ***Practical aspects.*** There are several practical matters that will need to be provided for. As the focus of the Review Panel recommendation is on speedy, cheap alternative dispute resolution, there should be an emphasis on informality in the Panel's operation. In particular, the Panel should not be bound by the rules of evidence. The Panel should have to give reasons for its decisions. To act as a filter against frivolous or vexatious applications for review, it should be a requirement that the member have first approached the scheme through the internal dispute resolution mechanism recommended above. However, where there is no internal mechanism for resolving disputes, the internal mechanism is not likely to be of assistance (because, for example, the trustees have exercised their discretion finally) or where there are other special circumstances, the Panel should be able to hear an application for review.

77. Under the Constitution, such orders may only be made by courts exercising the judicial power of the Commonwealth. They cannot be made by administrative agencies or tribunals.

78. In the case of LIFA, life companies and LIFA; in the case of the Banking Ombudsman, banks and the Banking Ombudsman Pty Ltd.

79. This Act only provides for review as to questions of law. The court cannot review the matter on the merits, or substitute its own decision. It is not possible to exclude, for either party, access to the prerogative writs: Constitution s 75(v); *Judiciary Act 1903* (Cth) s 33.

Recommendation 12.9: Superannuation Review Panel

1. The law should establish a Superannuation Review Panel, with the function of adjudicating disputes between members of superannuation funds or ADFs and the responsible entities of the funds.

2. The Panel should have no more than 3 members, appointed by the Minister on the nomination of interested groups. At least one member should have to have experience and knowledge of superannuation matters.

3. The Panel should be able to review any decision in relation to the member made by the responsible entity for the fund in the exercise or purported exercise of a power it has as responsible entity.

4. The Panel should only be able to make orders as follows:

- if the Panel finds that the power has been not been exercised improperly — an order affirming the decision
- if the Panel finds that the power has been exercised improperly
  - — an order referring the matter back to the responsible entity to reconsider the matter and make a fresh decision in accordance with directions given by the Panel
  - — an order varying the decision
  - — an order substituting for the decision its own decision.

Without limiting the circumstances in which the Panel may find that the exercise of a power by a responsible entity was improper, the Panel should so find if it finds that the responsible entity, in making the decision

- failed to take a relevant consideration or matter into account or
- took an irrelevant consideration or matter into account or
- acted in bad faith or with malice.

5. A member of a scheme should not be able to apply to the Panel unless

- he or she agrees not to take proceedings in equity in relation to the subject matter of the application, but the Constitution (that is, the prerogative writs (Constitution s 75(v)) and the ability to seek judicial review under the *Administrative Decisions (Judicial Review) Act 1975* (Cth), of the Panel's decision on the application, should not be affected

- **either**
  - **there is no internal review mechanism established for the scheme**
  - **the decision concerned has been reconsidered in accordance with the internal review mechanism established for the scheme or**
  - **the Panel determines that the internal review mechanism is unlikely to assist or there are special circumstances that justify the application being made.**

6. The law should provide that the conditions under which a superannuation scheme or an ADF attracts a tax concession include that the responsible entity must agree to be bound by any decision of the Superannuation Review Panel, but without prejudice to its rights to take proceedings under the Constitution (that is, the prerogative writs (Constitution s 75(v)) or *Administrative Decisions (Judicial Review) Act 1975* (Cth) in relation to the Panel's decision on the application.

Access to superannuation schemes

Qualifying periods

12.43. Many single employer sponsored superannuation schemes are not available to employees immediately upon commencing employment. A qualifying period of employment has first to be served.[80] The qualifying period is justified by employers on the basis of the administration costs involved in high turnover industries and because superannuation is designed as a reward for loyalty by employees to the enterprise and a qualifying period helps to reinforce this. In the past, superannuation qualifying periods were often different for women and men. The Review understands that in more recent times, industry practice has changed, and that this is no longer common practice. Furthermore, recent amendments to the *Sex Discrimination Act 1984* (Cth) will ensure that, as of June 1993, qualifying periods which discriminate either directly or indirectly on the basis of sex will be unlawful.[81]

80. There are minimal qualifying periods for the superannuation entitlements under awards and for superannuation provided in relation to the SGL legislation. Under the SGL legislation, it is proposed that employers be liable to provide superannuation for employers if they earn more than $300 in a seven consecutive day period or they earn more than $3000 in the financial year concerned: SGL Information paper, 6.
81. The Act was amended by the *Sex Discrimination Amendment Act 1991* (Cth) s 9.

Delayed vesting

12.44. Not all employer contributions to superannuation schemes vest, that is become the property of the employee, immediately. Member-financed benefits are required to vest immediately and in full. Contributions by employers pursuant to an industrial award vest immediately, as will the contributions made under the proposed SGL legislation. Other contributions made by employers vest only in accordance with the trust deed or other instrument constituting the scheme. In the case of accumulation schemes, an employee who leaves before the employer's contributions vest is only entitled to receive his or her own contribution and the fund's credited earnings rate (or some lower designated rate). In the case of defined benefit schemes a similar 'deemed' earnings rate is generally applied to the contributions of a member who leaves the scheme before any benefit from the employer has vested in the employee. The Commonwealth has proposed that, from 1 July 1995, the maximum period for vesting of employer contributions will be 10 years from the date of contribution.[82]

Problems and difficulties

12.45. Qualifying periods and deferred vesting pose significant problems for several groups of superannuation scheme members, particularly women and those in part time or casual employment. Quite apart from the gender differences built into wage and salary rates,[83] the structure of women's participation in the workforce, combined with typical qualifying periods and vesting provisions, mean that it generally takes longer for women than for men to achieve a comparable vesting level. In addition, breaks in employment, for maternity or other reasons, usually mean that the qualifying period, both to join the scheme and for vesting purposes, is interrupted and must often be recommenced at the next time of employment.[84] The restriction of superannuation to persons in paid employment[85] also limits the ability of women to save for their retirement.

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82. In 1989 the Minister for Social Security announced additional minimum vesting and preservation standards to come into question from 1 July 1995. These standards will require that all employer financed benefits accruing from 1 July 1995 vest in the employee at a rate of not less than 10% so that by the end of the tenth year with an employer there will be 100% vesting of those benefits: B Howe, *Better Incomes; Retirement Income Policy into the Next Century* 39.
83. Statistics for August 1991 show that average weekly earnings for females are 84.47% of those for males: Australian Bureau of Statistics, *Average weekly earnings, State and Australia*, August 1991.
84. See generally H Martin, *The Impact of the 1991 Budget Superannuation Reforms on Women*, speech to the Superannuation Agenda Conference, December 1991.
85. Contributions to superannuation schemes can only be made for up to two years following cessation of employment (full time or part time): OSS Regulations reg 5AA(3).

The ALRC is bound to have regard in its work to the Commonwealth's Access and Equity policy. The problems arising from delayed vesting and qualifying periods clearly involve issues that need to be considered in the light of that policy.

The Superannuation Guarantee Levy (SGL) legislation

12.46. In the 1991-92 Budget the Commonwealth announced its intention to impose a levy from 1 July 1992 on all employers who do not make a contribution to a superannuation scheme on behalf of all their employees. The amount of the levy will be equivalent to 3% or 5% of salary, depending on the size of the employer's payroll. This proportion will rise to 9% by the year 2000.[86] These contributions are to be fully vested in the employee and subject to a minimum qualifying period of employment.[87]

The Review's position

12.47. The ability of superannuation schemes to be a privately funded complement to the age pension will clearly be enhanced if the qualifying periods and vesting restrictions were reduced or eliminated, because a greater number of persons will receive superannuation benefits. The Review notes that the 10 year vesting schedule proposed by the Government in 1989 for contributions to superannuation schemes other than those made under the SGL legislation is to be reviewed in the light of the Government's policy announced in the 1991–92 Budget. Vesting of employer contributions should occur as early as possible. The Review proposed in DP 50 that there should be no qualifying periods for superannuation schemes other than a period sufficient to ensure that the administrative costs of establishing an account for a member do not outweigh the member's accrued benefits. SGL contributions will be payable after 7 consecutive days of employment during which earnings are $300 or more. The Review suggested in DP 50 that a similar regime exist for non SGL superannuation benefits.[88] It also proposed that all superannuation scheme deeds should, within a period of four or five years, provide for immediate vesting.[89] The Review understands from the ISC that the removal of all existing vesting restrictions and qualifying periods would add approximately 1% to wages costs

86. J Kerin, *1991–92 Budget Speech*, 11.
87. See fn 80.
88. DP 50 proposal 9.8.
89. DP 50 proposal 9.9.

for employers. The Review considered that the additional cost is justified on the public policy grounds stated above. The Review sought comment on whether this would have any adverse consequences, for example, whether employers may tend to underfund employer sponsored defined benefit schemes.

Submissions

12.48. ***No qualifying period.*** This proposal received significant comment. A number of submissions considered that, where employers voluntarily provide benefits in excess of the SGL legislation requirements, there is no justification for specifying a qualifying period for those additional benefits.[90] It was argued that if the qualifying period for voluntary contributions is aligned with that for SGL legislation contributions, employers will stop offering voluntary superannuation to any of their employees.[91] One submission suggested that the purpose of a qualifying period is to avoid the administrative expense of high turnover in early service where the administrative costs would dissipate a significant part of the benefit accruing and thus defeat the purpose of providing a benefit.[92] The proposal received support from a number of organisations.[93] The Securities Institute of Australia suggests that a qualifying period of three months would be more appropriate than the SGL legislation 7 days.[94]

12.49. ***Immediate vesting.*** A number of submissions disagreed with the proposal to introduce immediate vesting.[95] Most opposition focused around the argument that an employer voluntarily offering benefits should be able to impose whatever conditions he or she sees fit. Additionally, it was suggested that greater withdrawal benefits are likely to influence a fund's investment strategies.[96] Some submissions support the principle of immediate vesting but suggest that it should be phased in over a number of years.[97] Several submissions disagreed that immediate vesting is appropriate but indicated that a shorter period than 10 years would be appropriate.[98]

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90. eg Mercer Campbell Cook and Knight *Submission* February 1992.
91. D Knox *Submission* February 1992.
92. AMP Society *Submission* February 1992.
93. eg Jacques Martin Industry *Submission* February 1992; Permanent Trustee Company Ltd *Submission* January 1992.
94. Securities Institute of Australia *Submission* February 1992.
95. eg ASFA *Submission* March 1992; LIFA *Submission* March 1992.
96. See, eg, Mercer Campbell Cook and Knight *Submission* February 1992.
97. See eg, D Knox *Submission* February 1992.
98. See eg, Australian Friendly Societies Association suggested vesting should be phased in at 20% each year aiming at full vesting after five years: *Submission* February 1992; National Mutual believes that vesting over five to 10 years is appropriate: *Submission* February 1992.

12.50. ***Recommendation — qualifying period.*** The Review remains of the view that ideally, the qualifying period for the SGL legislation contributions and voluntary contributions should be the same. It does not accept that employers will stop offering voluntary benefits. The Review acknowledges there may be legitimate concerns with regard to the administrative costs of opening and closing membership 'accounts' for staff with very high turnover rates. The Review recommends, therefore, that the maximum qualifying period for voluntary superannuation schemes should be three months.

12.51. ***Recommendation — vesting.*** The Review remains of the view that immediate vesting should be required at some future time. The Review does not accept that the government has no right to impose vesting scales on voluntary contributions in excess of the SGL legislation requirements. The Commonwealth's policy is to encourage such superannuation with the concessions for the same ultimate purpose — namely to provide better retirement support income. It is of little benefit if the vesting scales determined by employers are so long that very few employees benefit from the scheme. Even if employers reduce the amount of superannuation offered to some employees, so as to keep their overall cost of superannuation the same, the distribution of benefits amongst the workforce will be more equitable. For the moment, the Review accepts that there is significant opposition to this principle and that a reasonable lead up period must be provided before any change is made. Accordingly, the Review recommends that schemes should provide by 1995 that employer contributions should vest at 20% a year (that is, total vesting, within five years of being made).

Recommendation 12.10: Qualifying and vesting periods

1. The law should provide that the conditions under which a superannuation fund attracts a tax concession include that the qualifying period for access to benefits under the scheme be no more than 3 months. This should be phased in over 3 years.

2. The law should provide that the conditions under which a single employer sponsored or industry superannuation fund attracts a tax concession include that employer contributions to the fund in excess of those to be required under the Superannuation Guarantee Levy Bill 1992 vest in the employee at the rate of 20% each year. This requirement should be introduced in 3 years.

Unclaimed benefits

Introduction

12.52. As compulsory contribution rates increase and vesting periods decrease, more members, especially those with broken work patterns, will accrue benefits. This, combined with an increasingly mobile workforce, will mean that the possibility for schemes to 'lose' members who are entitled to benefits will increase. DP 50 noted that this made it important that mechanisms be established to deal with unclaimed benefits in a way that will maximise the prospect of members receiving contributions made on their behalf. While increasing community awareness about superannuation means that more people will be aware of their obligation to preserve the superannuation benefits they receive on termination and of the consequent need to keep the scheme informed of their address, it is likely that schemes will lose contact with a growing number of members.

Procedures for locating members

12.53. ***DP 50 proposal.*** Each superannuation scheme should establish a set procedure to minimise the chance of losing members. One possibility suggested was that schemes ask joining members to nominate a rollover fund into which they would like their benefit paid should they leave the job without notifying the scheme. The members should have appropriate information about this mechanism. DP 50 also raised the possibility of establishing standard procedures for schemes trying to locate lost members, including obtaining access to the members' tax file number (TFN). DP 50 proposed that the scheme be exempt from requirements to report to a lost member whose address has been proven to be not current in accordance with a standard procedure.[99]

12.54. ***Submissions and recommendations.*** Most submissions supported this proposal in principle.[100] Submissions that addressed the issue of access to TFNs drew attention to the need to ensure that the Information Privacy Principles in the *Privacy Act 1988* (Cth) are adhered to.[101] One submission pointed to the particular importance of this proposal for casual workers:

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99. DP 50 proposal 9.10; see recommendation 10.28.
100. eg Norwich Group *Submission* February 1992; AMP Society *Submission* February 1992; ASFA *Submission* March 1992; Women's Economic Think Tank *Submission* February 1992.
101. Australian Taxation Office *Submission* February 1992; DSS *Submission* February 1992.

> Our worry is that casual and part time workers, who are often female will be lost if there is not some system for central collection of such funds and relation to tax file number, with a responsibility on the agency to find the member. There must be a continuing obligation on funds to chase members with some entitlements over a set amount if there is no government alternative.[102]

Given the support the proposal received, the Review recommends that it be adopted. For greater certainty, the procedure should accord with guidelines issued by the regulator. The mechanism for requiring compliance will have to be access to tax concessions. However, because of the importance of retaining restricted access to the tax file numbers, the Review is not proceeding with the suggestion that responsible entities be given access to tax file numbers.

Recommendation 12.11: Unclaimed benefits procedure

1. The law should provide that the responsible entity for a superannuation fund or ADF, and the provider of a DA, must establish a procedure, conforming to guidelines published by the regulator by notice in the *Gazette*, for finding members of the scheme who do not claim benefits that are due to them, or whom the responsible entity or provider cannot locate.

2. The law should provide that the responsible entity for a superannuation scheme must ensure that each member booklet, prospectus or offer document for the scheme include particulars of this procedure.

Unclaimed benefits arrangements

12.55. *A single register.* Any scheme to deal with unclaimed benefits should be designed to maximise the possibility of those benefits being claimed. DP 50 noted the Review's view that this will best be achieved if, as well as the scheme mechanisms just recommended, there is established a single, central register of unclaimed benefits. People would then know exactly where to go to check whether any money is being held on their behalf. DP 50 proposed that the regulator establish such a scheme.[103] It would be called an Unclaimed Benefits Fund (UBF). Suggestions were made concerning its administration, including that the management of the UBF be contracted out. The regulator would nevertheless maintain a central register of 'lost' members. DP 50 also noted that the ISC has for some time been working on devising a scheme to deal with unclaimed benefits, involving the establishment of specialist schemes (Automatic Rollover Funds — ARFs) into which lost benefits would automatically be

102. Women's Economic Think Tank *Submission* February 1992.
103. DP 50 proposal 9.11.

transferred. That proposal does not, however, appear to provide for a central register to be kept nor does there appear to be any limit on the number of ARFs. DP 50 explained that the Review considers such a proposal as less likely to result in lost funds being returned to their owners than the Review's proposal.

12.56. ***Submissions.*** Very few submissions opposed the UBF proposal. ASFA was concerned at the regulator's involvement.

> A relevant consideration, particularly in a review of the prudential framework, is the question of who would control the proposed single fund (ie who is the responsible entity) and to whom is that entity answerable. ASFA is concerned at the review suggestion that the regulator should be responsible for the UBF. A regulatory agency is ill-equipped to take the commercial decisions involved in contracting the administration and investment activities and in balancing the (often conflicting) interests of members.[104]

It also expressed support for a vehicle along the line suggested by the ISC's proposal:

> ASFA believes that a small number of ARFs (or similar), together with a centralised register, might achieve most of the economies available from a single UBF (or similar) and would aid in creating a competitive environment to maximise returns and minimise costs. Furthermore, if it is accepted that some form of automatic rollover is an efficient way of dealing with preserved benefits (particularly relatively small ones), then it should be noted that many members would be happy to accept such arrangements where the trustees of the scheme chose the rollover vehicle, but would not be happy for the amount to automatically go to a central, regulator-run fund.[105]

Most other submissions supported the proposal.[106] It was said that the databases of many funds would need to be improved for the system to function effectively.[107] A number of submissions were concerned to ensure that there would be no, or only a limited, compulsion to transfer money to the UBF.[108]

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104. ASFA *Submission* March 1992.
105. ASFA *Submission* March 1992.
106. eg Jacques Martin Industry *Submission* February 1992; Permanent Trustee Company Ltd *Submission* February 1992; Westpac Financial Services *Submission* February 1992; The Securities Institute of Australia *Submission* February 1992; Shell Australia Ltd *Submission* February 1992.
107. Australian Taxation Office *Submission* February 1992.
108. eg Mercer Campbell Cook & Knight *Submission* February 1992; Office of the Cabinet (Qld) *Submission* February 1992.

12.57. ***Recommendation.*** A system along the lines proposed in DP 50 will be needed. There are a number of issues that need to be clarified.

- ***Administration and management.*** The Review did not intend that the UBF become a large government run ADF. It was intended that the government's role would be restricted to a clearing house of information and contributions. All the administration and management should be awarded by tender to private sector suppliers. To reinforce this point the proposal is referred to below as the Unclaimed Benefits System (UBS). So long as the administration and the management of the funds in the UBS are tendered out to independent professional administrators and investment managers, the concerns expressed by ASFA in relation to the regulator's involvement should be met.

- ***Transferring money to the UBS.*** The UBS should be able to accept money from responsible entities for superannuation schemes or ADFs, and they should be legally able to transfer the money to the UBS, at any time after six months after the member has become 'lost'.[109] The law should require the responsible entity of a scheme to transfer the money to the UBS after a member has been lost for two years.

- ***Fees and charges.*** The administration costs of the UBS should be paid out of the gross earnings of the funds in the UBS.

- ***'Lost' members.*** A member should be regarded as 'lost' if, using the mechanism recommended above,[110] the responsible entity has been unable to locate him or her and at least six months have passed.[111]

- ***Returning members.*** When a 'lost' member is located, the amount standing to the member's credit should be notified to the member and have the same status as an ETP.

Recommendation 12.12. Unclaimed benefits

An arrangement for an unclaimed benefits scheme (UBS) should be established as an ADF. However, disclosure requirements, reporting to member requirements and member representation requirements should not apply to the UBS. The law should provide for a UBS as follows:

109. If the scheme is not an 'eligible' scheme, ie, does not attract tax concessions, there should be no bar on its transferring money for lost members — defined by the scheme — to the UBS.
110. Recommendation 12.11.
111. See recommendation 10.28.

- **the regulator should keep a register of 'lost' members notified to it by responsible entities**
- **the regulator should not manage or administer the money covered by the UBS and should regularly put these functions out to competitive tender.**
- **the UBS, or its agents, should be able to accept money from any scheme**
- **the administration costs of the UBS should be paid out of the gross earnings of the funds in the UBS**
- **the responsible entity for an eligible superannuation scheme or eligible ADF**
  - **may transfer unclaimed benefits to the UBS after the member has been lost (to their scheme) for six months and**
  - **must transfer unclaimed benefits to the UBS as soon as practicable after the member has been lost (to their scheme) for a total of two years.**

Small amounts to reserves?

12.58. It has been suggested that small amounts, for example, of up to $100, are not worth keeping for a member who is lost and should be counted as part of a scheme's reserves. Some trust deeds presently provide for this. DP 50 suggested that all amounts, no matter how small, ought to be transferred to the UBS.[112] It may happen that several small amounts will be transferred for the one person and combine to make a worthwhile sum. To provide otherwise would eliminate any chance that the accrued benefit may one day be obtained by the member. If, after cross checking with the DSS and the ATO, the UBS does not succeed in locating a particular member by the time that person would have reached a specified age,[113] that money should be used to fund the administration of the UBS. However, it can be expected that with the establishment of the UBS there will be fewer and fewer lost benefits. Most submissions agreed with this approach.[114] It is important to preserve for members as much as possible of their retirement benefits. The Review confirms its proposal in DP 50.

112. DP 50 proposal 9.12.
113. DP 50 suggested 66 years: para 9.40.
114. AMP Society *Submission* February 1992; Westpac Financial Services *Submission* February 1992; Securities Institute of Australia *Submission* February 1992; Women's Economic Think Tank *Submission* February 1992; ASFA *Submission* March 1992.

Recommendation 12.13: Unclaimed benefits not to be put to reserves

The law should provide that it is an offence for the responsible entity for a superannuation fund to transfer the amount of benefits not claimed by the members entitled to them to the reserve established for the fund.

Hardship cases

12.59. ***Proposal.*** Superannuation benefits over $500 are preserved until the member reaches the age of 55.[115] Access to benefits before retirement is generally not permitted. However, most deeds provide for early release of preserved benefits at the trustee's discretion, because of hardship. It could be argued that the early release of money specifically designed to provide for retirement income directly contradicts the purpose of superannuation. ASFA considers that access to benefits in the event of hardship should not be allowed.[116] DP 50 proposed that so long as the terms of the trust deed provide very strict criteria for the proof of hardship, early release of benefits ought be permitted in extreme circumstances.[117]

12.60. ***Submissions.*** A number of submissions agreed with this proposal,[118] which is a restatement of the present situation, but many expressed concern about the need for rigidly defined criteria for the assessment of early releases on the grounds of hardship.[119] Some suggested that no hardship releases should be allowed in any circumstances

> [T]he current high level of early payments is in our view negating member respect for the preservation requirements. It reflects the impossibility of trustees, of large funds in particular, and a regulator satisfactorily sorting out the cases which are genuine.... These problems can only be resolved by removing the right to seek release in the case of hardship. Retirement benefits are for use in retirement and the community will not appreciate [that] this is the case if preservation requirements are treated lightly.[120]

115. OSS Regulations regs 9, 10, 11, 12.
116. ASFA *Policy Issues Paper* 1991, 57.
117. DP 50 proposal 9.13.
118. AMP Society *Submission* February 1992;
119. eg Jacques Martin Industry *Submission* February 1992; KPMG Peat Marwick *Submission* February 1992.
120. Mercer Campbell Cook & Knight *Submission* February 1992.

The Review understands that the ISC is also concerned about the increased number of requests for early release on the grounds of hardship.[121] This increase is no doubt a direct reflection of the current poor economic climate. Nevertheless, permitting such payments represents a significant encroachment on the retirement incomes policy. It is clear that the assessment of early releases is a time consuming and often very difficult task; one that neither trustees nor the ISC seem keen to do. The Review understands that the ISC proposes to involve trustees to a much greater degree in the assessment process.

12.61. ***Recommendation.*** The Review is concerned that the objectives of the Commonwealth's retirement incomes policy may be threatened by the early release of benefits. Even with a tightening of the criteria and the procedure for applying[122] there can be no guarantee that this does not happen. The burden on trustees and the regulator is also significant, although the Review acknowledges that the demand for early releases is somewhat cyclical. Accordingly, it recommends that trust deeds should not be able to permit early releases on the grounds of hardship. A transitional period should be allowed for trust deeds that currently provide for such releases.

Recommendation 12.14: Hardship cases

The law should provide that a provision in the deed or other instrument constituting a superannuation fund that permits a member to withdraw money from the fund, on the ground of hardship is of no effect.

Bankruptcy

Bankruptcy of member

12.62. Currently, many superannuation deeds provide that, if a member becomes bankrupt, the member's benefits under the scheme are forfeited to the fund. The trustees often have an absolute discretion whether to use the money for the benefit of the bankrupt or their dependants, to reduce the employer's contributions in respect of other members or otherwise for the benefit of other members. The Review regards this situation as inequitable. It is inconsistent with the aims of retirement incomes policy. The question is how to balance the needs of the bankrupt for retirement income support with the policy of divisibility of the bankrupt's property for the satisfaction of creditors. The Review

121. The ISC received 4,700 applications for early release of benefits in 1989/90, about 12,000 in 1990/91. It expects to receive between 25,000 and 30,000 requests in 1991/92. The Review understands that about 75% of applications for release of preserved benefits are approved.

122. eg requiring applicants to sign a statutory declaration as to their financial affairs.

recommends that the law should prevent a bankrupt member's vested benefits, so far as they represent contributions made in satisfaction of the SGL, being forfeited to the scheme. Instead, they should be applied by the responsible entity to buy an annuity for the member, either immediate or deferred (depending on the member's age). The income from the annuity should be treated as protected income under the *Bankruptcy Act 1966* (Cth).[123] A deferred annuity should not be counted as an asset of the member. This recommendation will mean that members will, consistent with the Commonwealth's retirement incomes policy, benefit from their superannuation. Similar considerations might apply to the amount in the member's account that represents the excess over SGL contributions. It is important that the protection of the kind just recommended is not used by individuals to escape their proper liability to their creditors by making large contributions to their superannuation scheme just before they are declared bankrupt. Superannuation benefits which relate to contributions in excess of those made pursuant to the SGL legislation should not, therefore, be automatically protected. The trustee in bankruptcy of the bankrupt's estate should be able to apply to the court for an order requiring the responsible entity to release to the receiver the contributions in excess of the SGL contributions that have been made on behalf of the bankrupt within the previous two years.[124] The same regime should apply to deposits in ADFs and DAs.

Recommendation 12.15: Bankruptcy of scheme member

1. The law should provide that, except as recommended below, on bankruptcy of a member of a superannuation fund or an ADF, none of the amount standing to a person's account in the fund or ADF is capable of being taken by the trustee in bankruptcy as part of the person's estate.

2. The law should provide that, on becoming aware that a member of the superannuation fund is bankrupt, the responsible entity for the fund must apply so much of the amount standing to a person's account in the fund as represents the contributions required to be made under SGL, and the earnings thereon, to buy an annuity for the member, either immediate or deferred (depending on the member's age).

3. The law should provide that the income from the annuity is protected income under the *Bankruptcy Act 1966* (Cth) and that the deferred annuity is not property of the member divisible among the creditors.

123. See *Bankruptcy Act 1966* (Cth) s 116(e), (f), (fa).

124. This equates with the period recommended by the ALRC in its report *General Insolvency Inquiry* (ALRC 45, 1988) as the period for relation back in respect of transfers to associates.

4. A court having jurisdiction in bankruptcy should be able, on application by the trustee in bankruptcy or the Official Receiver of a bankrupt's estate, to declare, by order, that some or all of the amounts standing to a bankrupt's account in a superannuation fund or ADF that is

- **more than the amount referred to in 2 and**
- **represents contributions made within the previous two years, and the earnings thereon,**

is property divisible among creditors.

Bankruptcy of employer

12.63. Another issue relating to bankruptcy about which the Review is concerned is the bankruptcy, or liquidation, of an employer sponsor. The employer's receiver will be placed in the employer's shoes in relation to the superannuation scheme. The receiver will be placed in a difficult position involving a potentially significant conflict of interest between its duty to the creditors and its duty as a member of the responsible entity board to the members of the scheme. Concern has been expressed to the Review that the employees are more likely than not to be the losers when such conflicts arise. The only way to ensure such conflicts do not arise is to require the appointment of a temporary independent person as the responsible entity of a single employer sponsored scheme as soon as the employer is placed in liquidation. Accordingly, the Review recommends that, when an employer entitled to appoint at least 50% of the members of a responsible entity board is placed in liquidation, the board of the responsible entity should be replaced by a temporary independent responsible entity.

Recommendation 12.16: Bankruptcy of employer

The law should provide that the regulator, on becoming aware that the employer in a single employer sponsored superannuation fund has become bankrupt or, in the case of a company, become an externally administered body corporate, must, by written instrument, remove the responsible entity from office and appoint another responsible entity in its stead.

Superannuation on divorce or separation

Significance of family law issues

12.64. The main focus of this reference is on the proper regulation of superannuation schemes and the prudential requirements which should apply. While it is not absolutely essential in the context of this reference to deal with questions concerning the property rights of married people or de factos, there are good reasons to do so. It has been recognised in the Commonwealth's retirement incomes policy that superannuation entitlements are generally intended to provide for the needs of both parties, and the spouse of a member does make a (non-monetary) contribution to superannuation.[125] It is desirable that the fairness which is intended to flow from the retirement incomes policy extend to the partner of the contributing member. The Review has considered significant aspects of the relationship between the members of superannuation schemes and the responsible entities. The changes necessary to achieve justice between partners to a marriage will affect that relationship. Finally, the recommendations made earlier to require incorporation of most schemes will put it beyond doubt that there is constitutional power to deal with the issue, a problem which has up to now precluded a satisfactory resolution of the problem.[126]

The issues

12.65. There are two main issues. The first is what principles should apply to the allocation of interests in superannuation funds between parties to a marriage, or to a de facto relationship. The second issue is how to implement this principle in the most effective way.

General principles that should apply

12.66. ***Present law.*** Under the present law, the Family Court has an almost unfettered discretion to alter the property interests of spouses who separate or divorce. The Court may

> make such order as it thinks fit altering the interests of the parties in the property [of the marriage].[127]

No property is excluded. However, it has been held that until a superannuation entitlement matures in the hands of the beneficiary it is not property and cannot be dealt with directly.[128] Nevertheless, under the *Family Law Act 1975* (Cth)[129]

125. Howe *Better Incomes: Retirement Incomes Policy into the Next Century.*
126. See ALRC 39 para 467-8; the Attorney-General's Department's Discussion Paper *The Treatment of Superannuation in Family Law* (1992) argues that, although the marriage power is sufficient in the case of spouses, that power does not extend to the case of de factos spouses: para 37-8.
127. *Family Law Act 1979* (Cth) s 79(1).
128. *In the Marriage of Crapp* (1978) 32 FamLR 286; *Evans v Public Trustee (WA)* (1991) FamLR 646.
129. s 75(2).

it is a relevant financial resource to be considered when determining property rights between the spouses. This limits the court in the kind of orders it can make, though it does not necessarily affect the principles of sharing which are addressed here.

12.67. ***Equal sharing principle.*** The superannuation entitlements of the spouse who is a member of a superannuation scheme have been built up over a working life. However, superannuation is usually a valuable joint matrimonial asset to which both parties have contributed directly or indirectly. One of the parties will frequently have acted to his or her disadvantage by relying for security on the prospective superannuation entitlement of the spouse. The Family Court generally takes the view that, because the parties have, in effect, given up current income for future security they should both be regarded as contributors to the superannuation fund.[130] This view was reflected in the *Better Incomes* statement of the Minister for Social Security:

> [W]omen who work at home — as well as those paid in employment — contribute to their spouse's superannuation. However, they do so by providing household services and by giving up current income.[131]

The Review accepts the principle, set out in the ALRC's report *Matrimonial Property*, that, unless the circumstances are exceptional, the contributions that spouses make to the economic life of a marriage should be regarded by the law as equal.[132] This is particularly so for superannuation entitlements which are wholly related to the spouses' employment. This means that the portion of the superannuation entitlements that is attributable to the period of the spouses' cohabitation should be seen as the joint product of the spouses' equal efforts. The Review takes the approach that the principle upon which this entitlement ought to be divided on separation or divorce is that of equal sharing.

Implementation

12.68. ***Present problem.*** The main problem under the present law is to find a satisfactory way to implement the principle of equal sharing. The reason is that superannuation cannot usually be dealt with as property; even if the interest has fully vested, the amount may not be ascertainable. The unsatisfactory situation

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130. eg *In the Marriage of Bailey* (1979) 33 FamLR 10; *In the Marriage of Crapp* (1978) 32 FamLR 286; *In the Marriage of Lalor* (1989) 14 FamLR 282.
131. Howe, *Better Incomes: Retirement Incomes Policy into the Next Century* 25.
132. ALRC 39 para 350.

regarding superannuation was recognised by the Family Law Council[133] and by the first Joint Select Committee on the Family Law Act in 1980.[134] In 1987, the ALRC recommended a straightforward formula to deal with superannuation, under which the notional value of a spouse's benefit in a superannuation scheme would be included in the property to be divided between the parties.[135] The formula included a method of working out the value of the superannuation. The basic value is the amount which would be paid to the spouse if he or she resigned from the superannuation scheme on the date selected by the court.[136] If the spouses had lived together for the whole period of contribution to the scheme, the basic value worked out in the way described would be the value to be divided. If the period of contribution had commenced before the relationship, or extended beyond it, the amount to be divided would be a proportion of the basic value. For example, if the couple lived together for 7 years, and the spouse had contributed to the scheme for 10 years, 7/10ths of the basic value would be included in the property for division. These recommendations establish a clear method of valuation and enable other property to be divided more equitably. They do not, however, create any direct interest in a superannuation scheme for a spouse or partner of the member. To this extent they are not adequate to implement the Commonwealth's retirement incomes policy.

12.69. *Splitting the fund.* A better objective for which the law ought to strive in this area is to divide the contributing spouse's entitlement in the fund (or that part of it which is attributable to the relationship) into two. Each spouse could then have the benefit of one of these shares as a continuing interest in the superannuation fund. Such an approach to the reallocation of superannuation benefits will achieve the following goals of policy in this area.

- ***Equity.*** It will be equitable as between the spouses and will recognise the equal contributions of each spouse.

- ***Supporting retirement income.*** It will give the non-contributing spouse the opportunity to have a superannuation entitlement which he or she can add to or roll over into another scheme and thus be in keeping with retirement incomes policy.

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133. Family Law Council, Working Paper No 8 *Superannuation and Family Law* (1980). The Family Law Council in 1980 recommended joint Commonwealth and State legislation to provide that divorced wives and all children be included as beneficiaries in all super schemes; to make orders of Family Court enforceable.

134. Joint Select Committee on the Family Law Act, report *Family Law in Australia*, 95–7.

135. ALRC 39.

136. ALRC 39 para 469. If the superannuation is taken as a pension, it is given a lump sum value for this purpose.

In 1987 the ALRC considered the prospect of splitting the funds in a similar way. It concluded at that time that such a proposal was not warranted.[137] Since then, however, the position has changed markedly. The Commonwealth's retirement incomes policy has been established and superannuation is an integral and important part of that policy. The Review considers that the reservations expressed in 1987 by the ALRC should be re-examined.

12.70. ***Legislative power.*** One reason why the ALRC did not recommend that a spouse be given a direct interest in the superannuation entitlements of the partner, or that the court be given power to order an assignment of an interest in a scheme which would bind the trustees, was the lack of constitutional power. The recommendations made earlier in this report[138] will overcome this problem by requiring superannuation schemes which seek tax concessions to have an incorporated responsible entity or to bring themselves within the ambit of the Commonwealth's power in respect of old-age and invalid pensions. This will remove the objection.

12.71. ***Delay in finalising the financial relationship.*** Another issue raised by the ALRC in its earlier report was the undesirability of delaying the financial settlement until the spouse who was a scheme member retired or died. This objection recedes in importance when the implications of the retirement incomes policy are bought into account. Superannuation is intended to provide a supplement to retirement incomes and is a long term interest. Ways need to be explored of preserving the interests of both parties without keeping them tied together financially as a result.

Submissions

12.72. Most submissions which dealt with this issue supported the Commission's approach.[139] Those who did not thought the matter fell outside the ambit of the Review's terms of reference or that the formula would be difficult to apply. Those who supported the proposal made a number of suggestions, for example, to consider tax consequences, to clarify the formula and to consider contributions before and after marriage.

137. ALRC 39 para 467–8.
138. Recommendation 7.1.
139. eg Australian Shareholders' Association *Submission* February 1992; IFA *Submission* February 1992; Permanent Trustee Company Limited *Submission* February 1992; DSS *Submission* February 1992.

Application to different kinds of schemes

12.73. ***Treatment of entitlements in accumulated schemes.*** The application of the principle of equal sharing in the case of entitlements in an accumulation scheme presents few problems. The responsible entity could to be required to determine the amount to be credited to an account for the non-contributing spouse. That account should have credited to it an amount equal to half the amount in the scheme standing to the credit of the contributing spouse. If the scheme represents in part contributions made before or after cohabitation, an appropriate apportionment would be made. The contributing spouse's share in the scheme should be decreased accordingly. The non-contributing spouse's entitlement should be 'rolled over' into an ADF or similar superannuation scheme. Nothing in the deed or other instrument establishing the scheme should be able to inhibit this. In particular, provisions restricting membership of the scheme to particular occupations, or employment with a particular employer, and provisions that give the responsible entity a discretion to exclude or vary an entitlement, should be ineffective in this context.

12.74. ***Treatment of entitlements in defined benefit schemes.*** Entitlements in defined benefit schemes present more difficulties. As with accumulation schemes, the responsible entity ought to be required to determine the amount to be credited to an account for the non-contributing spouse. That amount should in principle represent one half of the contributing member's entitlement accrued during the period of cohabitation. But as the amount may be difficult to ascertain, a formula will need to be devised, to take into account the particular circumstances of the scheme and the way the defined benefit is calculated.[140] If possible, that formula ought to be prescribed in legislation in accordance with the principle which has been outlined. In any event, deeds and other instruments creating defined benefit schemes ought in future to include provision for such a formula. The effect of the formula ought to be to credit the non-contributing spouse with the amount, worked out under the formula, and to reduce the contributing spouse's entitlement accordingly. As with accumulation schemes, the non-contributing spouse's entitlement should be 'rolled over' into an ADF or similar superannuation scheme. Appropriate provision could be made to enable this amount to be ascertained. The deed or other instrument establishing the scheme should not be able to inhibit the creation of the new account.

12.75. ***Variation of shares.*** Under the present law the court has a complete and unfettered discretion to adjust the parties' shares in their property. In its report

140. This formula could be based on the formula that will have to be devised under the SGL legislation to calculate the prescribed maximum level of employer superannuation support: see SGL Information paper, Appendix B.

on *Matrimonial Property*[141] the Commission recommended that this broad discretion be replaced with a structured discretion, under which the court would apply a basic rule of equal division of property. The ALRC recommended that, while the basic rule was equal division, the parties should be able to make their own arrangements for the division of their property on separation or divorce. Subject to strict safeguards as to fairness, these arrangements would be enforceable.[142] Should the court or the parties be able to vary the shares proposed above? The Review is of the view that they should. There may be cases where appropriate superannuation arrangements for the non-contributing spouse can be made without the need to disturb the contributing spouse's entitlement, as, for example, where there are enough funds otherwise available to buy the non-contributing spouse an appropriate superannuation entitlement in another scheme. The restrictions as to fairness of the agreement proposed by the ALRC should remain, but should be strengthened by the inclusion of a further, specific consideration: whether the net result of the arrangement proposed would be to leave the non-contributing spouse without appropriate superannuation coverage. To ensure that this provision is respected, agreements should be subject to court approval. The court should also have a limited power of adjustment, taking into account the factor just mentioned.

Attorney-Generals' Department Discussion Paper

12.76. ***Deemed reallocation.*** In a Discussion Paper published in March 1992, the Attorney-General's Department proposed a statutory scheme under which

> As from the date of permanent separation, the contributing spouse's superannuation entitlement would be deemed by statute to have been reallocated between the parties. Parties who did not want the deemed reallocation to apply would have to seek court approval to depart from the statutory scheme.[143]

The grounds of departure would be limited. This scheme would avoid the need for a court application unless the parties could not agree, or wanted a different, or no, superannuation arrangement. On the other hand, the facts which the trustees would need to know (such as relevant dates) would not be readily ascertainable unless either the parties or the court made a formal assignment. The trustees would be required to provide information to the non-contributing spouse. While the proposed formula provides for equal division, it would do so without regard to the way in which the other property of the parties was dealt with. It would apply only to vested funds.

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141. ALRC 39.
142. ALRC 39 ch 10; see also ALRC DP 46, para 3.70.
143. Para 27.

12.77. ***Comparison with DP 50 proposal.*** The principles behind the Attorney-General's Department proposal are similar to those the Review has put forward. The main difference is that they would operate without a court order, though a court might need to make an assignment if the parties could not agree. The Review proposes that the matter always be dealt with by court order or by court approval of an agreement. The grounds for allowing a court to depart from equality are limited in each case and require consideration of each party's superannuation positions. The Attorney-General's Department's proposal would apply only to vested funds, whereas the Review proposal could be adapted to apply to any superannuation interest, even before vesting and before the amount of the interest was known. The non-contributing spouse could not acquire an interest or prospective interest that was more than the appropriate proportion of the interest achieved by the contributing spouse.

Recommendation

12.78. The Review has considered this question in the light of submissions received and of the more recent proposals in the Attorney-General's Department Discussion Paper. It has concluded that the principles upon which the superannuation entitlements of spouses ought to be re-arranged on separation or divorce is the principle of equal sharing recommended by the ALRC in its 1987 report. There are some attractions in trying to devise a mechanism for prescribing, in legislation, the way in which superannuation should be divided. The Review agrees with the thrust of the proposals in the Attorney-General's Department's discussion paper, that parties should, in relation to their superannuation as in relation to other kinds of property, be encouraged to resolve matters without the need for court adjudication. But its view is that court oversight is still desirable. The re-allocation of superannuation arrangements on divorce or separation should continue to be subject to court control. The principal reasons for this are

- the desirability, from the responsible entity's point of view, of having a clear, simple and authoritative statement of the entitlements that need to be dealt with or created
- the need for court control where some variation of the general rule proposed is wanted by the parties and to ensure that the final re-allocation of superannuation entitlements is fair having regard to all the circumstances.[144]

144. Additionally, reallocation under a court order is required in order to ensure that the re-allocation does not create capital gains tax liabilities: ITAA s 160ZZM, 160ZZMA.

In other respects the Review confirms the proposal in DP 50 and recommends accordingly.

Recommendation 12.17: Superannuation on divorce or separation

1. The *Family Law Act 1975* (Cth) should be amended to empower a court exercising jurisdiction in proceedings with respect to the property of parties to a marriage to direct the responsible entity of an accumulation scheme of which one of the parties is a member to split the account of the contributing spouse and roll the amount (if any) awarded to the non-contributory spouse into an ADF. The proportion of the fund allocated to the non-contributory spouse should, unless the court orders otherwise, be half the value of that part of the fund accumulated during cohabitation. The ADF must be fully preserved. The order should have to be obeyed despite anything in the deed or other instrument establishing the scheme.

2. The *Family Law Act 1975* (Cth) should be amended to empower a court exercising jurisdiction in proceedings with respect to the property of parties to a marriage to direct the responsible entity of a defined benefit scheme of which one of the parties is a member to pay the entitlement of the non-contributing spouse, determined by the court, into an ADF. The entitlement of the member should be divided between the parties according to a prescribed formula.

3. The court should be able to depart from the prescribed shares (that is, 50/50 for accumulation schemes, as prescribed for defined benefit schemes) in limited circumstances. The parties should be able to vary the shares by agreement, subject to the protection recommended in the ALRC's report *Matrimonial Property* (ALRC 39) and subject to court approval. In deciding whether to depart from the prescribed shares, or to approve an agreement to that effect, the superannuation position of the non-contributing spouse should be considered.

4. The transfer should not be subject to any tax or duty.

De factos

Background

12.79. The reasons which make it important to deal fairly with the superannuation entitlements of married persons when they divorce or separate apply with equal force when persons in a de facto relationship separate. Several jurisdictions now have legislation allowing a court to distribute the property of parties to some de facto relationships when the relationship breaks down. These laws, however, do not apply throughout Australia, and are not uniform. In DP 50 the Review proposed that courts exercising jurisdiction under those laws should have the same powers as were recommended for courts exercising jurisdiction under the Family Law Act.[145] Very little comment was made on this proposal in submissions. Such comment as was made raised the same matters as were raised in relation to married persons.[146]

Recommendation

12.80. It would be undesirable for the law on this matter to apply differently in different parts of Australia. Responsible entities for schemes that operated on a national basis would face additional costs. There would be inequities between members of the same scheme who were in different jurisdictions. The earlier recommendations that are designed to ensure either that responsible entities incorporate as trading or financial corporations, or that schemes offer old-age pensions, will ensure that the Commonwealth will have constitutional power to legislate with respect to entitlements in these schemes, whether they are held by married persons or persons in de facto relationships. Given that retirement incomes policy has as much interest in adequate levels of post-retirement income for persons in de facto relationships as it does for married persons, the Review has concluded that the same principles ought to apply to the reallocation of superannuation entitlements on the breakdown of a de facto relationship as have been recommended for divorce or separation of married persons. The basis of that re-allocation is fair, and the Review sees the need to ensure enhanced levels of post-retirement income as the primary public policy goal in this area. Accordingly, the Review recommends that the law should provide that the parties to a de facto relationship are entitled and required to share the superannuation entitlements related to the period of their cohabitation on the same basis as that recommended for married persons. Again, a court order, or court approval of an agreement, should be required. The Review suggests that the Family Court be given jurisdiction in these matters, but that State and Territory Supreme Courts, which already have jurisdiction, either in their general equitable jurisdiction or under specific legislation in those jurisdictions where it has been enacted, should continue to have jurisdiction. The question which court should have jurisdiction was not raised by the Review in DP 50 and the Review expects that the Commonwealth will consult with the States and Territories before legislating to implement this recommendation.

145. DP 50 proposal 9.14.

146. eg Women's Economic Think Tank *Submission* February 1992.

Recommendation 12.18: Superannuation and breakdown of de facto relationships

The law should provide that, on the breakdown of a de facto relationship, the superannuation entitlements of the parties to the relationship should be re-allocated on the same basis as provided for in recommendation 12.17. Jurisdiction in respect of proceedings under this recommendation should be conferred on the Family Court, the Family Court of Western Australia and on the Supreme Courts of the States and Territories.