7.3 SUPERANNUATION

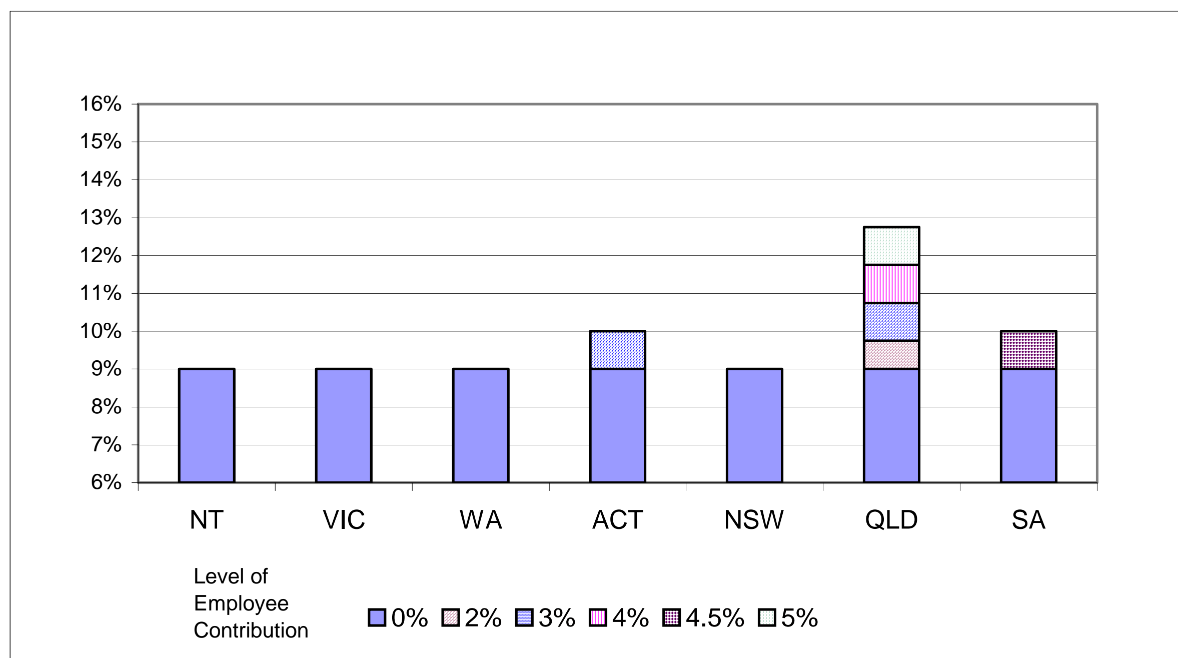
The 2006-07 Budget contains significant measures to place the ACT public sector's superannuation arrangements on a sustainable footing. From 1 July 2006, new employees will receive superannuation benefits that match those offered by other state and territory governments.

In addition, the Government has brought forward the target for fully funding the ACT public sector's superannuation liabilities to 1 July 2030. This target is consistent with the majority of state and territory governments. The previous target was to fund 90 per cent of superannuation liabilities by 2040.

New employees joining the ACT public service from 1 July 2006 will receive an employer superannuation contribution of 9 per cent of their eligible superannuation salary. This is the same level as offered by almost all state and territory governments. The Government will also provide an additional 1 per cent contribution for employees who contribute 3 per cent of their salary to superannuation. This is more generous than all other state governments with the exception of Queensland. Arrangements are in place to allow employees to make their contribution by way of salary sacrifice.

Additionally, the Government will be similarly taking steps to reduce the superannuation arrangements applying to new Members of the Legislative Assembly, Legislative Assembly Members' staff, judges and magistrates, Senior Executives and Senior Office Holders.

Figure 7.3.1
Maximum level of Employer Contribution given the level of Employee Contribution



Note: Queensland still provides access for new employees to a defined benefit superannuation scheme. The level of employer contribution to the accumulation scheme, as outlined above, is equivalent to the level of notional employer benefit provided under the defined benefit scheme.
Examples from the chart: For Queensland, if the employee makes a contribution of 2 per cent, the level of employer contribution increases from 9 per cent to 9.75 per cent, if the employee contributes 3 per cent, the level of employer contribution increases from 9 per cent to 10.75 per cent. For Victoria, no matter what the level of employee contribution is, the employer will only contribute a maximum of 9 per cent.
The level of ACT employer contribution to the PSSap is not dependent on the level of employee contribution.

It is important that the ACT's superannuation arrangements are placed on a sustainable footing. Cash payments to meet the Territory's superannuation obligations to its current and former employees are projected to grow very strongly. By 2020 these cash payments will total $265 million (in 2005-06 dollars).

Table 7.3.1 below summarises estimated cash payments to be made over the period 2006-07 to 2009-10.

Table 7.3.1
Estimated Superannuation Payments

30 June	Defined Contribution $'000	Defined Benefit CSS $'000	Defined Benefit PSS $'000	Total $'000
2007	14,500	46,100	15,100	75,700
2008	23,300	49,900	18,000	91,200
2009	32,800	53,800	20,900	107,500
2010	43,200	58,100	24,800	126,100

Note: The CSS and PSS projected superannuation payments exclude the employer productivity payments, which range between 2 per cent and 3 per cent of salary, made directly to ComSuper on behalf of the employee. These payments will approximate $20 million per annum over the Budget and forward years but will be declining over time as CSS and PSS members retire or leave the ACT public service.
The estimate for payments in relation to the defined contribution schemes (PSSap and Fund of Choice) are based on assumptions in relation to the level of ACT Government staff employee turnover and appropriate salary level. The cash flow profile will change to the extent that actual outcomes differ from these assumptions. The PSSap and Fund of Choice payments will be made each fortnight to the complying superannuation funds and will extinguish the Territory's liability.

ACT Government superannuation arrangements for employees can vary due to the date of employment, type of employment, or specific agency. The main superannuation arrangements for most permanent ACT Government employees include the Commonwealth Superannuation Scheme (CSS), the Public Sector Superannuation Scheme (PSS), and the Public Sector Superannuation Accumulation Plan (PSSap). A default superannuation scheme for new employees joining the ACT public service from 1 July 2006 will be determined shortly following a competitive tender process.

From 1 July 2005 the PSS closed to new members and all new permanent ACT employees employed after that date became members of the PSSap. The scheme design is a defined contribution plan (accumulation) arrangement where the employer is required to contribute 15.4 per cent of superannuable salary and to continue to meet scheme administration costs.

From 1 July 2006, the Territory is required to introduce full superannuation fund choice for all new employees. Employees will have the choice of joining the default fund or another fund that they may prefer.

Both the PSSap and the default arrangements are fully funded defined contribution (accumulation) schemes. This means that the employer contribution will be fully met at the time the liability arises. The estimated cost of funding the PSSap and the 'choice' arrangements is shown in Table 7.3.1. The discussion in the rest of this chapter, relating to the outstanding superannuation liabilities and assets, refers to the now closed CSS and PSS schemes.

The estimate of payments for the CSS and PSS are provided by the Government's consulting actuary. These annual payments are made quarterly in advance to the Commonwealth (ComSuper) on behalf of the ACT Government.

Defined Benefit Superannuation Schemes

With effect from 1 July 1989, the ACT Government became a separate body politic and is responsible to the Commonwealth for the employer-financed portion of superannuation benefits provided to employees for their period of employment with the ACT Government. This employer-financed component is the total benefit payable less the accumulated member and employer productivity contributions with interest.

Both the CSS and PSS incorporate defined benefits, which means that benefits payable to members are defined in advance according to certain formulas, based on such factors as years of service, final average salary, and the annual level of employee contributions.

The CSS closed to new members from 1 July 1990. The CSS is a hybrid defined benefit scheme, in the sense that it incorporates both a defined benefit and an accumulation benefit. Like the PSS, it is only a partially funded scheme with the employee contributions and the employer productivity contributions paid to the scheme administrator. Employee contributions of five per cent to the scheme are mandatory. The CSS was primarily designed as a pension based benefit scheme.

The PSS was opened on 1 July 1990, and was compulsory for all ACT Government employees employed in a permanent capacity. The PSS is a partially funded defined benefit scheme, with mandatory annual employee contributions of a minimum of two per cent to a maximum of ten per cent, and the employer productivity superannuation contribution paid to the scheme administrator. The scheme was primarily designed as a lump sum payment arrangement, but a pension option is also available. The PSS closed to new members from 1 July 2005.

The CSS and PSS are administered on behalf of the Territory and Territory employee members by the Commonwealth agency, ComSuper. ComSuper also administers the new PSSap scheme. For more information on the CSS or PSS, the ComSuper website is http://www.comsuper.gov.au.

Superannuation Provision Account (SPA)

The Superannuation Provision Account (SPA) was established in 1991 to assist the Government in managing its superannuation liabilities. The SPA is not a superannuation scheme for ACT Government employees, but an ACT Government account to receive appropriations and make payments in connection with the Government's defined benefit CSS/PSS employer superannuation liabilities.

The operations of the SPA are subject to the legislative requirements of the *Territory Superannuation Provision Protection Act 2000* and the *Financial Management Act 1996*. The Territory Superannuation Provision Protection Act legislation limits moneys standing to the credit of the SPA to be used for superannuation purposes only, not for the general purposes of Government.

The SPA receives annual appropriations from the ACT Budget. Payments for emerging cost (benefits) to the Commonwealth and administration costs are made from the SPA.

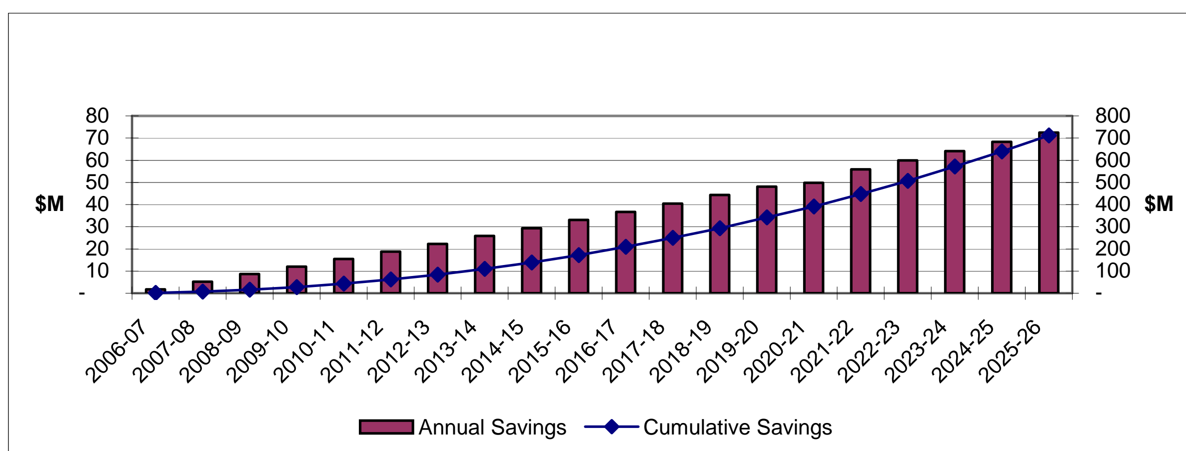
Superannuation Funding

The Government is committed to the effective management of superannuation liabilities through a funding plan that is reviewed periodically. Employer contribution levels are also periodically re-assessed to ensure they are consistent with the underlying full cost of the two superannuation schemes. The Government has previously committed to fund 90 per cent of accrued superannuation liabilities by 30 June 2040. This target date has now been brought forward, with the aim of funding 100 per cent of superannuation liabilities by 2030.

This target will require very substantial, and growing, cash payments for superannuation - both to meet the need to fund superannuation accumulation benefits as they occur and to provide cash injections into the Superannuation Provision Account (SPA).[1]

The measures announced in the 2006-07 Budget, to bring superannuation contributions into line with the general standard in other jurisdictions, are a critical component of the strategy to achieve this new funding target. As shown in Figure 7.3.2 they will provide significant savings over the next twenty years. These savings are essential to provide the capacity to support ongoing cash injections into the SPA.

Figure 7.3.2
Estimated Savings from Changed Superannuation Arrangements



[1] The cash injections required to be made into the SPA, to meet the Government's long term funding target, are revised each year to take account of updated actuarial and other assumptions. The 2006-07 Budget estimates take account of:

- the need for the Government to fund accumulation benefits each year to employees engaged after 1 July 2005 (this factor was not incorporated in the 2005-06 Budget estimates, pending the review of the long term funding objective); and
- the outcomes of the triennial actuarial review and subsequent changes in the long term bond rate.

The defined benefit superannuation liabilities for ACT Government employees are a substantial portion of all General Government Sector (GGS) liabilities, currently over 65 per cent of all liabilities. As at the end of the 2005-06 financial year these liabilities will total approximately $2.9 billion. The investment assets set aside to meet these projected liabilities will total approximately $1.8 billion. The Territory will therefore have an unfunded position of $1.1 billion, or a funded percentage of 62 per cent, going into the 2006-07 Budget year. The funded percentage is estimated to grow to 63 per cent by the end of the 2006-07 Budget year.

Based on the latest Budget projections, incorporating the reviewed superannuation funding plan, it will take approximately another 23 years to reduce the unfunded gap to zero, or to reach a funded percentage of 100 per cent.

The 2006-07 Budget estimates for the SPA are shown below in Table 7.3.2.

Table 7.3.2
Annual Funding and Accruing Liability

30 June	Employer Contributions $'000	Annual Budget Injection $'000	Net Investment Earnings $'000	Total Receipts $'000	Annual Accruing Liability $'000
2006	13,400	125,200	252,500	391,100	405,200
2007	0	124,300	137,300	261,600	260,900
2008	0	109,700	151,100	260,700	257,800
2009	0	112,400	165,100	277,500	260,700
2010	0	115,200	179,700	294,900	262,100

Note: The 2005-06 accruing liability incorporates an additional actuarially determined increase in liabilities at 30 June 2006 of $178.3 million, to take account of the new Australian equivalent to International Financial Reporting Standards (AIFRS), as well as the triennial actuarial review of all financial and demographic assumptions.
The employer contribution figure includes Government Business Enterprise and Statutory Authority contributions. The annual accruing liability figure is the annual increase in the outstanding employer superannuation liability for employees who are members of the CSS and PSS. From 2006-07 the main source of funding is through annual capital injection by Government. All notional employer contributions made by agencies in relation to the defined benefit liabilities are directed to the Territory Bank Account.

The accruing liability figure represents the growth in liabilities from year to year and is made up of the annual service and interest cost, less actual benefit payments. The service cost is the increase in the present value of the defined obligation resulting from employee service in the current period (in other words, it measures the cost of superannuation for existing employees in a given year). The interest cost is the increase during a period in the present value of a defined benefit obligation, which arises because the benefits are one period closer to settlement (in other words, it measures the interest cost on superannuation liabilities for former and existing employees that were accrued in previous years).

In nominal terms, and based on the current actuarial determination, the superannuation liability is now estimated to peak at approximately $8.1 billion by 30 June 2035.

The funding level of superannuation liabilities is forecast to increase slowly over the forward estimated period, illustrated in Table 7.3.3, following the increase in unfunded liabilities in 2005-06 due to the triennial actuarial revision. Further details on the revisions made to estimated superannuation liabilities as a result of the latest triennial actuarial review are provided later in this chapter and in the 2005-06 Budget Mid-Year Review.

Table 7.3.3
Percentage funding of liabilities

30 June	Assets $'000	Liabilities $'000	% Funded
2006	1,799,300	2,886,200	62%
2007	1,995,000	3,147,100	63%
2008	2,183,400	3,408,800	64%
2009	2,381,600	3,665,600	65%
2010	2,589,000	3,927,800	66%

Note: The figures exclude both the estimated MLA and Totalcare superannuation liabilities, which are not material when compared to the defined benefit CSS/PSS superannuation liability estimates.

Superannuation Assets

The investment assets held by the SPA include Australian and international money market securities, Australian and international fixed interest securities, Australian and international equities, Australian private equity, and Australian direct unlisted property. These investment assets are projected to grow over time through the injection of funds by Government (capital injections) and the reinvestment of all earned income.

These financial assets are invested and managed according to an asset allocation strategy that takes into account the risk/return objectives of the Territory and the long-term nature of the superannuation liabilities and projected cash flow requirements.

The Superannuation Unit does not undertake investment management in-house. External, asset specific, institutional fund managers are appointed to manage the Territory's financial assets. The individual investment management agreements prescribe all of the allowable investments that may be entered into in accordance with the *Financial Management Act 1996* and the *Territory Superannuation Provision Protection Act 2000.*

The Superannuation Unit also utilises the services of an appointed Asset Consultant, a Master Custodian and a Finance and Investment Advisory Board. Further information on the assets set aside for superannuation purposes is outlined in Chapter 7.2 Investments.

Superannuation Liabilities

The value of accrued superannuation liabilities is calculated as the present value of the future payment of benefits that have actually accrued in respect of service at the calculation date. This approach, which is known as the 'actual accruals' basis, is in line with accepted international accounting practice.

The 2006-07 Budget for the Superannuation Unit incorporates the latest triennial actuarial review of the Territory's superannuation liabilities, conducted by the Government's consulting actuary, using salary and membership data as at 30 June 2005. An actuarial review is conducted annually, which updates for both salary and membership data and the discount rate, but the financial and demographic assumptions are only reviewed and revised every three years.

This report sets out the following key results:

- projections of the Territory's accrued superannuation liabilities in respect of ACT Government employees who are members of the CSS or PSS defined benefit schemes; and
- annual payments that should be made by the Territory to the Commonwealth to discharge its superannuation liability with respect to benefits currently payable to members. These recommended payments are known as the emerging cost payments.

The ultimate cost of a defined benefit plan (final benefits to employees) is influenced by many variables and is therefore uncertain. This uncertainty is likely to persist over a long period of time. Accounting for defined benefit plans is therefore complex because actuarial assumptions are required to measure the obligation, and the expense, and there is a possibility of actuarial gains and losses (these arise when actuarial assumptions are different from actual outcomes). The obligations are measured on a discounted basis because they may be settled many years after the employees render the related service.

The calculation of accrued superannuation liabilities and the projected stream of emerging cost payments therefore require many assumptions about the future membership of the CSS and PSS. Actuarial estimates of superannuation liabilities are based on a wide range of economic, financial and demographic assumptions. These assumptions include general salary increases, CPI, promotional increases in salary, resignation, retirement, invalidity, mortality, mortality of pensioners and future mortality improvements, benefit stream election (lump sum, pension or both), and level of PSS member contribution.

The actuarial financial and demographic assumptions used for the latest triennial actuarial report were completely reviewed and revised, where appropriate, based on past membership experience.

The key differences in the financial assumptions in the current projections from those adopted for the previous Territory actuarial report include:

- an increase in the PSS pension election assumption from 50 per cent to 70 per cent to better reflect actual scheme experience;
- an increase in the PSS employee contribution rate from 5 per cent to 5.9 per cent to better reflect actual scheme experience; and
- adoption of the Australian equivalent to International Financial Reporting Standards (AIFRS) which requires reference to a Government long term bond rate as the appropriate discount rate at the time of review. The discount rate is meant to reflect both the estimated average timing of benefit payments and the time value of money. In the past the discount rate has been set as a long term assumption by the Actuary. The discount rate was reduced to 5.5 per cent. As the discount rate reduces, the valuation of liabilities increases.

The financial impact of the triennial actuarial review, as reported in the 2005-06 Budget Mid Year Review, was an increase in the projected superannuation liability as at 30 June 2006 of $319.4 million, of which $43.8 million was expensed in 2005-06.

On 3 May 2006, the Reserve Bank of Australia (RBA) increased the target cash rate by 0.25 per cent to 5.75 per cent. As a result of the impact of this decision on the level of the ten-year Commonwealth Government bond yield, the actuarial liability valuation has been revised in the 2006-07 Budget to reflect a discount rate of 5.75 per cent.

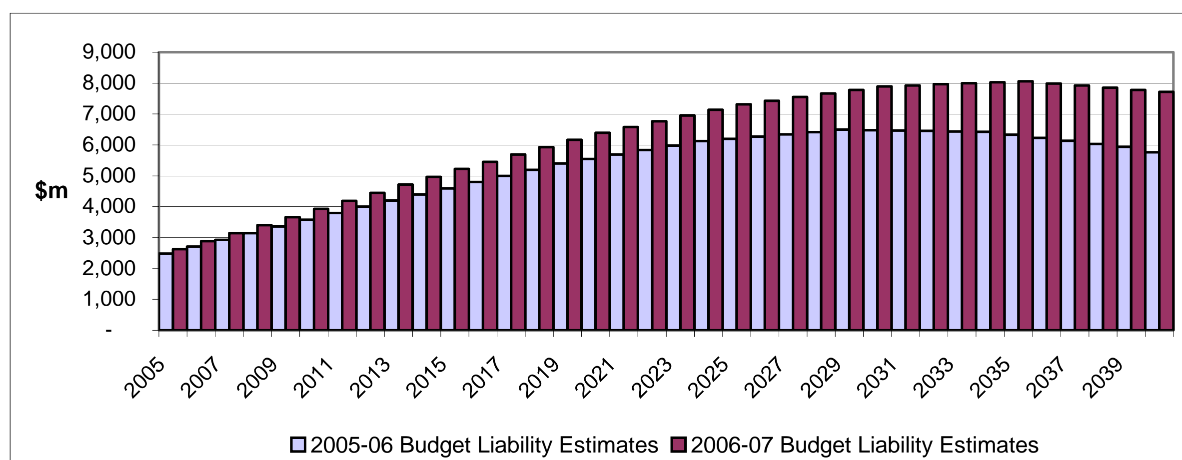
Relative to the estimates published in the 2005-06 Mid Year Review, the revision to the discount rate has resulted in a decreased defined benefit liability valuation as at 30 June 2006 and decreased annual superannuation expenses as detailed in Table 7.3.4. The revised impact on the superannuation liability as at 30 June 2006 is now $178.3 million of which $31.1 million has been expensed in 2005-06.

Table 7.3.4
Revised Estimated Superannuation Liabilities and Expenses arising from the Triennial Actuarial Review

	Estimated Actuarial Loss at 30 June 2006 $'000	Change to Estimated Superannuation Expenses 2005-06 $'000	Total Change in Estimated Superannuation Liability at 30 June 2006 $'000
Mid Year Review	275,600	43,800	319,400
Revised	147,200	31,100	178,300
Total Decrease	128,400	12,700	141,100

The impact to the estimates for the Territory's projected superannuation liabilities due to the triennial actuarial review and revision to the discount rate are illustrated in Figure 7.3.3.

Figure 7.3.3
Actuarial Revision to Estimated Superannuation Liabilities



Over time, actual outcomes in relation to compensation growth, staff turnover, length of service, level of employee contributions, mortality, disability, inflation and the preference for lump sum benefits over pensions will vary from what has been assumed by the actuary. To the extent that these occur, there will be changes in the cash flow profile for the Government.

Totalcare Employees

Past Totalcare employee records and information are being finalised and all required obligations relating to past and current employees will be met by the Government.

The current superannuation liabilities of the Territory incorporate an estimate in relation to the obligation to Totalcare employees of $17.3 million. Payments in relation to these obligations are budgeted to be made over the 2006-07 Budget and forward years. As these payments are made on a progressive basis, the liability will be re-assessed and appropriate adjustments will be made to the current estimate.