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This document prepared by the late Mr Allan Archer, which has June 2002 on its cover sheet, was obtained through a Freedom of Information (FOI) application made after the Ombudsman's Report had been tabled in the Legislative Council on 2 July 2014. The report referred to 'actuarial worksheets' of which SA Superannuants, Richard Vear and Barry Foster had been unable to obtain copies and which they had suggested might be non-existent. The Ombudsman reported that copies of the worksheets had been shown to him by a witness who had described them as worksheets that had been included in a package of materials provided to the treasurer in June 2002 to assist him with his decision about EISS rules. However, the Ombudsman did not retain a copy of these 'actuarial worksheets' and did not provide any detail of the contents in his report.

On page 1 in its introduction this document makes clear that the changes to EISS rules had to meet two constraints not just the one constraint that member after-tax benefits must not be reduced. The additional constraint was that reductions could not be so high that they reduced employer costs.

On its page 23 the document is dated 5 September 2002 and so cannot have been provided to the Treasurer in June 2002. **It is clearly a document prepared after June 2002.**

On page 5 in the first paragraph under the heading 'Maximum Practical Benefit Reductions' it is stated that the maximum taxation reductions to benefits that could be made without any member suffering a reduction to his/her benefit have been outlined. This paragraph includes the statement that there is a later section demonstrating that these maximum reductions to benefits are required to prevent employer costs increasing. However, there is nothing in the document that demonstrates this for pensions.

In the second paragraph on page 5 it is stated that the approach to benefit reductions differs according to four different categories of benefit. The categories listed are- a lump sum rolled over to another fund; a lump sum paid in cash; a pension transferred to the state scheme; a pension paid from the scheme. It is then stated that these cases are considered separately below but there is nothing in the document about the taxation reductions that were to be made to pensions.

This document therefore resembles the June 27, 2002 Explanatory Memorandum, also produced by the late Mr Allan Archer, in that it implies coverage of taxation reductions to pensions but contains nothing specific about this class of benefit. Both of Mr Archer's documents acknowledge that the rules inserted by the Treasurer were not permitted to reduce benefits to an extent that reduced employer costs but neither document contains anything substantial to support his claims that employer costs for pensions would not be reduced by the method he recommended for the reduction of pensions .

(1)

Tax Reductions to Benef
June 2002
Electricity Industry Superannua
Scheme

MERCER
Human Resource Consulting

MMC Marsh & McLennan Companies

Introduction

The purpose of this report is to document the results of the actuarial analysis in respect of the tax reductions to the benefits provided by the Electricity Industry Superannuation Scheme. These reductions arise as a consequence of the Scheme losing its constitutional protection and thus becoming taxed.

Clause 11 of Schedule 1 of the Electricity Corporations Act 1999 gave the SA Treasurer the right to reduce the benefits provided by the Scheme upon the Scheme becoming taxed. There are two limits to the extent of these reductions:

(a) the reductions must **not reduce** the net benefits which Scheme members receive after tax – Clause 11(3);

(b) the reductions can only **avoid or reduce an increase** in employer costs – Clause 11(2) – which means that the reductions cannot be so high that they reduce employer costs.

Attached as an appendix are the rule changes made by the Treasurer to reduce the benefits. In my opinion:

- these rule changes do not reduce members; net benefits after tax; and
- based on the assumptions made, they do not reduce employer costs.

The following sections provide detail on these two matters.

Background

The Electricity Industry Superannuation Scheme was previously listed in the income tax legislation as a "constitutionally protected scheme".

By regulation made by the Commonwealth on 29 May 2002 (Statutory Rules 2002 No. 111), the Scheme lost its constitutional protection with effect from 1 July 2000. The Scheme therefore became a taxed complying superannuation fund as from that date. The Scheme is deemed to be a complying superannuation fund by virtue of still being an "exempt public sector superannuation scheme".

Clause 11 of Schedule 1 of the Electricity Corporations Act 1994 allows the Treasurer to vary the rules of the Scheme following the Scheme's loss of constitutional protection in order to avoid or reduce an increase in employer costs caused by the taxation changes arising from the Scheme's loss of constitutional protection. As part of the privatisation process, the Treasurer indicated to the tenderers that he would vary the rules so as to avoid an increase in employer costs, to the extent permitted by a constraint contained in Clause 11.

This constraint is that a rule variation which reduces benefits may **not** result in the level of the net benefits received by members being less than the level of their net benefits had the Scheme not lost constitutional protection – refer Clause 11(3). This constraint is further defined in Clause 11(8) by specifying that the comparison between net benefits before and after taxation is carried out on certain assumptions regarding taxation on benefit payments.

Clause 12 provides a mechanism whereby a Scheme member can appeal against the application of the rule variation on the ground that it reduced his/her net benefits.

Benefit Reduction Formulae used since 1 July 2000

As from 1 July 2000 **lump sum benefit payments** from the Scheme have been reduced on account of taxation on an interim basis and paid out as "taxed benefits", *ie* as benefits paid from a "taxed" source. This action was taken with the knowledge of the Commonwealth and State Treasuries on account of the delay by the Commonwealth in ceasing the constitutional protection while it waited to pass legislation to impose tax at the time of loss of constitutional protection.

The formulae used since 1 July 2000 for the benefit reductions were designed to ensure that each exiting member receives after tax at least the same amount as would have been received after tax had the unreduced benefit been paid out as an "untaxed benefit", *ie* a benefit from an "untaxed" source. In order to have a workable system, assumptions were made for the purpose of the reduction formulae. To the extent to which situations exist that do not conform to the assumptions, members end up with higher net benefits than before.

The reductions made to lump sum benefits since 1 July 2000 are the "maximum practical reductions: defined in the next section of this report.

No reductions have been made to any **pension payments** since 1 July 2000 since all pensions have been paid from the State Pension Scheme which retains its tax-free status. The pensions paid from the State Scheme are all "non-rebateable".

Payment of Tax on Loss of Constitutional Protection

In late 2001, the Commonwealth Government passed legislation to impose a tax at the time of loss of constitutional protection. This legislation (s. 281A of ITAA 1936) required the Scheme to include as part of its 2001 taxable income the "specified rollover amount" which would be included in its tax return had all accumulated member benefits been paid out of the Scheme on 30 June 2000 and rolled back into the Scheme on 1 July 2000. In my certificate dated 20 June 2002, I advised that this specified rollover amount totalled $41,504,000.

Tax on this amount at 15% is $6,225,600.

Pre July 1988 Funding Credits

At the end of May 2002, the Scheme received from APRA confirmation of a Pre-July 1988 Funding Credit (PJFC), which allows tax credits on account of the unfunded nature of the Scheme when superannuation funds in general become taxed in July 1988. The amount granted was $258,000.

The extent to which these tax credits can be utilised each year depends upon whether employer contributions paid to the Scheme in that year exceed the sum of the post 1983 part of the benefits paid by the Scheme over the year. Unused PJFC is indexed with AWOTE each year.

3

Maximum Practical Benefit Reductions

The purpose of this attachment is to outline the maximum taxation reductions to benefits could practically be made without any member suffering a reduction to his/her after tax benefit. A later section demonstrates that, subject to some adjustments, these maximum reductions are required to prevent employer costs increasing on account of the Scheme becoming taxed.

The approach differs by whether benefit is a lump sum rolled over to another fund, a lump sum paid in cash as an Eligible Termination Payment (ETP), a pension transferred to the State Scheme, or a pension paid from the Scheme. Those cases are considered separately below:

(a) Rollover of a Lump Sum to Another Fund

Where a lump sum benefit is rolled over to another superannuation fund, that fund must be advised the pre and post June 1983 components and the undeducted contributions (UDCs).

When the Scheme was constitutionally protected, the advice to the rollover fund needed to state that the post June 1983 component in excess of the undeducted contributions (*ie* specified rollover amount) was "untaxed". The rollover fund was required to pay tax at 15% on this specified rollover amount.

Now that the Scheme is taxed, the specified rollover amount is advised as coming from a taxed source and thus is not subject to tax in the rollover fund.

The maximum benefit reduction that can be applied to a rollover amount, without the member being disadvantaged, should be such that the amount retained in the rollover fund is the same in both cases. Hence the reduction is the amount of tax which the rollover fund would debit if the benefit were untaxed, *viz* 15% of the post June 1983 component in excess of the undeducted contributions.

To take an example, suppose:

- the gross benefit before reduction to be rolled over is $100,000;
- the post June 1983 service is 20 years and the total service is 25 years;
- the undeducted contributions total $20,000.

- If the Scheme were untaxed, the benefit of $100,000 would include an $80,000 post June 83 component, comprising $20,000 UDCs and a $60,000 untaxed benefit.
- The tax on rollover would then be 15% of $60,000, *ie* $9,000, leaving $91,000 in the rollover fund.
- Hence the benefit reduction is $9,000, giving a reduced benefit of $91,000.
- If this $91,000 is paid to the rollover fund as a "taxed" benefit, then the person would have $91,000 in the rollover fund as before.

The formula for the maximum benefit reduction (R) in the rollover situation is -

$$R = 0.15 \times (GB \times Post/Total - UDC)$$

where

GB	is the gross benefit before reduction
Post	is the number of days since the later of the eligible service date and 1 July 1983
Total	is the total number of days since the eligible service date
UDC	is the undeducted contributions.

(b) Payment of a Lump Sum in Cash as an ETP

Where a lump sum benefit is paid in cash as an ETP, the tax treatment depends upon whether the member is under age 55 or is age 55 or over, and, if age 55 or over, upon whether the benefit is under or over the tax-free threshold (currently $112,405), or is partly under and partly over the threshold.

When the Scheme was constitutionally protected, the post June 1983 component in excess of the undeducted contributions (*ie* specified rollover amount) was "untaxed". Now that the Scheme is taxed, the specified rollover amount is advised as coming from a taxed source.

The tax rates applicable to untaxed and taxed benefits are as follows:

	Member under age 55	**Member aged 55 & over**	
		Under threshold	**Over threshold**
Untaxed benefit	31.5%	16.5%	31.5%
Taxed benefit	21.5%	0%	16.5%

The maximum benefit reduction that can be applied to a cashable benefit amount, without the member being disadvantaged, should be such that the amount received in the taxed environment is the same as would have been received in the untaxed environment.

The general formula for determining the maximum benefit reduction (R) is therefore as follows (where the left hand side of the formula is the net amount received from the untaxed environment and the right hand side is the net amount received from a reduced benefit in the taxed environment):

$$GB - UR \times (GB \times Post/Total - UDC)$$
$$= (GB - R) - TR \times \{(GB - R) \times Post/Total - UDC\}$$

where:

GB is the gross benefit before reduction

UR is the tax rate for an untaxed benefit

TR is the tax rate for a taxed benefit

Post is the number of days since the later of the eligible service date and 1 July 1983

Total is the total number of days since the eligible service date

UDC is the undeducted contributions.

Rearranging the formula we obtain:

$$R = \{(UR - TR)/(1 - TR \times Post/Total)\} \times (GB \times Post/Total - UDC)$$

Using the tax rates shown in the above table, the reductions applicable to the three situations described above are:

- Cash payment to a member under age 55 (where UR = 0.315 and TR = 0.215):

$$R = \{0.1/(1 - 0.215 \times Post/Total)\} \times (GB \times Post/Total - UDC)$$

- Cash payment to a member age 55 or over where the entire benefit is under the threshold (where UR = 0.165 and TR = 0):

$$R = 0.165 \times (GB \times Post/Total - UDC)$$

- Cash payment to a member age 55 or over where the entire benefit is above the threshold (where UR = 0.315 and TR = 0.165):

$$R = \{0.15/(1 - 0.165 \times Post/Total)\} \times (GB \times Post/Total - UDC)$$

The following table shows values for the first part of these formulae for two extreme cases in respect of pre June 1983 service. The first case is where there is no pre June 1983 service (*ie* where "Post/Total" = 1) and the second case is where there is 20 years pre June 1983 service and 40 years total service (*ie* where "Post/Total" = 0.5).

	Factor in formula applied to "(GB × Post/Total – UDC)"	
	No Pre 83 Service	**20 Years Pre 83 Service**
Cash payment to member under 55	0.100	0.112
Cash payment to member 55 or over, where benefit is under the threshold	0.165	0.165
Cash payment to member 55 or over, where benefit is over the threshold	0.150	0.163

With these factors, the formulae will equate the net proceeds from untaxed benefits taken in cash with the net proceeds of taxed benefit taken in cash. However, in practice, a factor greater than 0.15 cannot be applied. This stems from the fact that although a benefit may able to be taken in cash, in many instances it will instead be rolled over to another fund. In fact, because of the working of the tax rates, there is an advantage to recipients of benefits from untaxed funds to firstly roll the benefit over to a taxed fund before accessing it in cash. In a rollover situation, the maximum reduction as earlier is 15% of the post June 83 part of the benefit in excess of the undeducted contributions, *ie* in algebraic terms -

$$0.15 \times (GB \times Post/Total - UDC)$$

At the time a benefit reduction needs to be calculated, it is not known whether the benefit will be taken in cash, or will be rolled over. Even the intended recipient may not know this at that stage. Furthermore, it is not practical to vary the reduction according to how much ends up being taken in cash. Thus it is necessary to adopt the **lesser** of the maximum reduction for a cash payment and the maximum reduction for rollover, to ensure that no one is disadvantaged.

Hence the maximum practical reduction for a member leaving when age 55 or over should be calculated using the 15% factor.

- ***Example – Member Aged 55 or Over***

To take an example, suppose as before:

- the gross benefit before reduction is $100,000;
- the post June 1983 service is 20 years and the total service is 25 years;
- the undeducted contributions total $20,000.

- If the Scheme were untaxed, the benefit of $100,000 would include an $80,000 post June 83 component, comprising $20,000 UDCs and a $60,000 untaxed benefit. Tax would be paid on this $60,000.
- Where the untaxed amount is rolled over, the tax deducted by the rollover fund is 15% of the untaxed $60,000, ie $9,000, thus leaving a net $91,000 in the rollover fund.
- If the payment is made instead as a taxed benefit, the benefit can be reduced by $9,000, giving a reduced benefit of $91,000.

The following table compares the result of paying the untaxed benefit with the result of paying the reduced taxed benefit:

	Benefit Taken in Cash by Member aged 55 & over	
	Under threshold	**Over threshold**
Untaxed Benefit - PAYG tax on benefit paid	16.5% of \$60,000 = \$9,900	31.5% of \$60,000 = \$18,900
- Net-of-tax cash benefit	\$90,100	\$81,100
Taxed Benefit - Benefit reduction	\$9,000	\$9,000
- Benefit after benefit reduction	\$100,000 - \$9,000 = \$91,000	\$100,000 - \$9,000 = \$91,000
- Post June 1983 component	Na	\$91,000 × 20/25 - \$20,000 = \$52,800
- PAYG tax on reduced benefit paid as a **taxed** benefit	na	0.165 × \$52,800 = \$8,712
- Net-of-tax cash benefit	\$91,000	\$82,288

This table shows that members who take their money in cash will gain from receiving a reduced benefit from a taxed fund – in the example, \$900 is gain for a payment under the threshold and \$1,188 is gained for a payment over the threshold. However the same gain could also be achieved by a benefit from untaxed source being passed through a taxed fund before being accessed in cash.

These examples ignore any income tax arising from 5% of the pre-July 1983 component being added to assessable income. Allowing for this would justify a higher reduction, the extent of which increases as the marginal tax rate increases. Given that we cannot know each member's marginal tax rate, it is reasonable to assume zero income tax on setting the benefit reductions, so no member will be thereby disadvantaged. This brings a small gain to those with pre-June 1983 service and paying income tax.

- ***Example – Member Aged Under 55***

The above example relates to members age 55 or over. The case of a member entitled to a cashable benefit when under age 55 also needs to be considered.

Suppose again:

- a gross benefit before reduction is \$100,000;
- post June 1983 service of 20 years and total service of 25 years;
- undeducted contributions of \$20,000.

- Applying formula above, viz:-

  R = {0.1/(1 - 0.215 × Post/Total)} × (GB × Post/Total - UDC)

  the benefit reduction is

  .1208 × (GB × Post/Total – UDC)
  ie .1208 × \$680,000 = \$7,246

Of course, a person who qualifies for a cashable benefit can always roll over the benefit to another superannuation fund. Again this can not be anticipated at the time a reduced benefit is calculated. The figures shown above indicate that, for a person under age 55, the lesser theoretical reduction occurs with a cash payment than with a rollover. Hence a person under 55 who rolls over a benefit which could be cashed will experience a lower reduction and hence a gain from the tax changes. The extent of this gain is shown in the following table (using the above example):

	Member under age 55 rolling over a cashable benefit
Untaxed Benefit	
- Tax when benefit rolled over	15% of \$60,000 = \$9,000
- Benefit in rollover fund	\$91,000
Taxed Benefit	
- Benefit reduction	\$7,246
- Tax when benefit rolled over	
- Benefit in rollover fund	\$92,754

This member has acquired \$1,754 through the change in the Scheme's taxation.

In summary, the formula for the maximum practical benefit reductions for a benefit which is cashable are:

- Where the member is age 55 or over:

  R = 0.15 × (GB × Post/Total – UDC)

  ie the same formula as for rollover

- Where the member is under age 55:

  R = {0.1/(1 - 0.215 × Post/Total)} × (GB × Post/Total - UDC)

(c) ***Payment of a Lump Sum, part of which is cashable and part of which must be rolled over***

In practice many lump sum benefits from the Scheme which have a cashable component will also have a preserved component which must be rolled over.

Where the member is aged 55 or over, the maximum practical reduction is calculated using the same formula with 15%factor.

Where the member is aged under 55, the maximum practical reduction needs to be calculated assuming that the member takes the cashable part in cash, even if that does not eventuate. This is necessary to ensure that no member is disadvantaged.

In the reduction calculations, the undeducted contributions need to be allocated between the two parts. Since undeducted contributions are invariably taken with the cash component, where part of the benefit is accessed in cash, it is satisfactory to calculated the reduction by including the undeducted contributions in a cashable component, to the extent possible.

In summary, the formula are as follows, where the member is age 55 or over:

R = 0.15 × (GB × Post/Total - UDC)

- Where the member is under age 55:

  R = {0.1/(1 - 0.215 × Post/Total)} × (GBc × Post/Total - UDCc) + 0.15 × (GBp × Post/Total – UDCp)

  where:

  GBc is the cashable part of the benefit before reduction

  GBp is the non-cashable part of the benefit before reduction

UDCc is the amount of the undeducted contributions up to a maximum of GBc × Post/Total

UDCp is an excess of the undeducted contributions over GBc × Post/Total

To take an example, suppose that for a member aged under 55:

- the gross benefit before reduction is \$200,000, of which \$120,000 may be taken in cash and \$80,000 must be preserved until retirement;
- the post June 1983 service is 20 years and the total service is 25 years;
- the undeducted contributions total \$90,000.

• In the untaxed situation, if the maximum cash is taken, (viz \$120,000), the tax on this is 0.315 × (\$120,000 × 20/25 - \$40,000), *ie* \$17,640. This gives a net-of-tax cash amount of \$102,360.

• Using the above formula, the benefit reduction is calculated as:

$$\{.1/C1 - 0.215 \times 20/25)\} \times (120,000 \times 20/25 - 40,000)$$
$$+ .15 \times (80,000 \times 20/25)$$
$$= 16,363$$

• Thus the benefit after reduction is \$183,637.

The following table compares the situation if the amount taken in cash is sufficient to give a net-of-tax amount in cash of \$102,360 (as above) or if only the undeducted contributions are taken in cash and the balance is rolled over.

	Member Under Age 55	
	Amount taken in cash to give \$102,360 after tax	**Only UDC taken in cash**
Untaxed Benefit		
- Gross Benefit	\$200,000	\$200,000
- Amount taken in cash	\$120,000	\$40,000
- Tax on cash payment	.315 × (\$120,000 × 20/25 - \$40,000) = \$17,640	-
- Net-of-tax cash benefit	\$120,000 - \$17,640 = **\$102,360**	**\$40,000**
- Amount rolled over	\$200,000 - \$120,000 = \$80,000	\$200,000 - \$40,000 - \$160,000
- Tax deducted by rollover fund	.15 × \$80,000 × 20/25 = \$9,600	\$160,000 - \$19,200
- Net amount retained in rollover fund	\$80,000 - \$9,600 = **\$70,400**	\$160,000 - \$19,200 = **\$140,800**

Taxed Benefit - Reduced Benefit	$183,637	$183,637
- Amount taken in cash	$113,237 *	$40,000
- Tax on cash payment	.215 × (113,237 × 20/25 - $40,000) = $10,877	-
- Net-of-tax cash benefit	**$102,360**	**$40,000**
- Amount rolled over & retained in rollover fund	$183,637 - $113,237 = **$70,400**	$182,637 - $40,000 = **$143,637**

* Chosen to give $102,360 net of tax

The first column of figures in this table shows that the member receives the same benefit after tax. The right hand column of the table illustrates that the member will gain if he/she takes a lower cash amount.

(d) ***Disability Lump Sum benefit***

The above analysis

	Member under age 55 Taking a benefit in cash
Untaxed Benefit - PAYG tax on benefit paid as an untaxed benefit	31.5% of $60,000 = $18,900
- Net-of-tax cash benefit	$81,100
Taxed Benefit - Benefit reduction	$7,246
- Benefit after benefit reduction	$100,000 - $7,246 = $92,754
- Post June 1983 component	$92,754 × 20/25 - $20,000 = $54,203
- PAYG tax on reduced benefit paid as a taxed benefit	0.215 × $54,203 = $11,654
- Net-of-tax cash benefit	$92,754 - $11,654 = $81,100

Thus the net-of-tax benefit is the sane whether it is paid as an untaxed benefit or as a reduced taxed benefit.

4

Actuarial Assumptions

1. Return on Investments, General Salary Increases and Pension Increases

The financial assumptions used for projecting the costs of the Scheme as from 1 July 2000 are equivalent to those used at the 29 February 2000 valuation of the Scheme.

Untaxed investment returns after expenses are assumed to average 4% pa ahead of price inflation (as measured by CPI). Investment returns after tax are assumed to be 0.6% pa lower than the pre-tax returns.

Salaries are assumed to average 1% pa ahead of CPI.

Pension supplementation is by definition, in line with CPI increases.

The actual assumptions used as from 1 July 2000 are:-

Investment Returns - untaxed and after expenses - after tax and after expenses		8% pa 7.4% pa
General Salary Increases		5% pa
Pension Increases		4% pa
Discount Rate - untaxed environment - taxed environment		8% pa (*ie* CPI+4%pa) 7.4% pa (*ie* CPI+3.4%pa)

(a) Investment Returns

Untaxed investment returns are used to project the Scheme costs on the assumption that the Scheme remained "constitutionally protected" from Commonwealth taxation.

The assumed investment return on the Scheme assets needs to take into account expected returns on each asset class, as well as the proportion of the Scheme in each asset class. The calculation is as follows:

Asset Class	Asset Allocation	Expected Return		Tax Effect
Australian shares	50.0%	9.1%	8.8%	0.3%
Overseas shares	25.0%	9.0%	8.0%	1.0%
Australian fixed interest	25.5%	5.8%	4.9%	0.9%
Overseas fixed interest	12.5%	5.7%	4.8%	0.9%
Portfolio – after administration fees of 0.3%		**8.0%**	**7.4%**	**0.6%**

Note: *The figures in this table are based upon advice received from Mercer Investment Consulting.*

(b) Discount Rate

The rates used for discounting the liabilities equal the assumed investment earnings, as previously and in accordance with Australian actuarial practice. Thus the present value of the Scheme liabilities calculated with this discount rate can be interpreted as the amounts of money which, if placed in a superannuation fund invested similarly to the Electricity Industry Superannuation Scheme, would on average be sufficient to cover the future cost of benefits accrued up to the valuation date.

2. Commutation Assumptions

The assumed extent of commutation exercised upon commencement of a pension is as follows:-

- Commutation on retirement of a contributor: 53% of the pension
- Commutation on commencement of a spouse pension: 43.25% of the pension

These assumptions are the same as these adopted in the 29 February 2000 actuarial valuation.

3. Interest Crediting Rate

The interest rate credited to member contribution accounts is assumed to equal the investment return, plus, for the Pension Scheme, an additional 4% in 2000/01 and 2001/02 and an additional 2% in 2001/02 to allow for the final allocation from the investment fluctuation reserve.

4. Other Assumptions

Rates of resignation and early retirement and rates of death and invalidity of contributors - Rates based on experience of similar funds – refer below for specimen rates.

Retrenchment - No retrenchments are assumed.

VSPs - No allowance is made for members leaving with a voluntary separation package.

Preservation – 90% of members of the Pension Scheme are assumed to take a preserved pension on resignation.

Rates of mortality of pensioners - Rates based on Australian Life Tables, adjusted in the case of retired contributors to reflect the assumptions for mortality used in the valuation of the State Pension Scheme - refer below for specimen rates.

Tax - No allowance is made for tax in the projections which assume that the Scheme will continue to be "constitutionally protected" from Commonwealth taxation. Tax on the Scheme at the rate of 15% as from 1 July 2000 is used in determining the costs with the Scheme taxed as from that date.

Expenses - The investment and administration expenses that are deducted from the investment return in setting the crediting rates have been allowed for in setting the assumed investment returns. The balance of the administration expenses and the expenses of effecting group life insurance are allowed for by grossing up the employer contributions necessary to cover the ongoing accrual of benefits.

5. **Sample Rates for selected ages:**

(a) Total and Permanent Disablement, Death and Resignation

Age last birthday x	Percentage of members age x at the beginning of a year assumed to leave the Fund during that year on account of -				
	Resignation	Death		Total and Permanent Disablement	
		Males	Females	Males	Females
	%	%	%	%	%
20	6.48	0.07	0.02	0.03	0.05
25	5.22	0.06	0.02	0.03	0.06
30	3.96	0.05	0.02	0.05	0.09
35	3.17	0.06	0.03	0.09	0.17
40	2.38	0.09	0.05	0.18	0.22
45	1.58	0.15	0.08	0.37	0.37
50	0.79	0.25	0.13	0.75	0.74
55		0.42	0.21	1.37	1.20

(b) Early Retirement

Attained Age x	Percentage of members age x at the beginning of a year assumed to leave the Fund during that year on account of early retirement %
55	10
56	8
57	11
58	16
59	31
60	100

(c) Mortality Rates of Age Pensioners

Age	Percentage of age pensioners aged x at the beginning of a year assumed to die during that year -	
x	Male Member %	Female Member %
55	0.43	0.25
60	0.75	0.39
65	1.32	0.67
70	2.33	1.24
75	4.10	2.34
80	7.14	4.41
85	11.76	8.18
90	18.12	14.46
95	25.52	22.10

(d) Mortality Rates of Members' Spouses

Age	Percentage of spouses aged x at the beginning of a year assumed to die during that year -	
x	Female Spouses %	Male Spouses %
50	0.25	0.42
55	0.41	0.72
60	0.65	1.24
65	1.05	2.06
70	1.75	3.29
75	3.03	5.31
80	5.25	8.50
85	9.02	12.98
90	14.86	18.62
95	22.10	25.52

(e) Mortality Rates of Invalidity Pensioners

Age	Percentage of invalidity pensioners aged x at the beginning of a year assumed to die during that year -	
	Males	Females
x	%	%
50	2.50	2.50
55	3.26	2.71
60	4.15	2.96
65	5.29	3.29
70	6.71	3.75
75	8.32	4.40
80	12.58	7.72
85	18.56	13.32
90	26.62	21.23
95	35.80	30.94

6. Age Differential of Member and Spouse

It is assumed that the spouse of an existing male pensioner will be 3 years younger, whilst the spouse of a female pensioner will be 3 years older.

5

Detail of the Rule Amendments

The purposes of the various elements of the Rule amendments are as follows:

Division 1

The amendment to **Rule 1** clarifies that the expression "investment return" means the return after allowing for tax (though Rule 30 modifies this effect in particular circumstances).

New **Rule 29** provides the mechanism for reducing gross benefits to the extent that net benefits are unchanged under certain assumptions. The assumptions are conservative in that they provide that members will not receive any net benefit lower than before, though some may receive higher net benefits according to whether their benefit payments are taken in cash, or rolled over, and according to their other income and benefits.

This approach of reducing benefits at the time of payment is applied to all Divisions 2, 3, and 4 members and to the benefits payable from Division 5 in 2000/01 and 2001/02. Division 5 members in the Scheme on 1 July 2002 are treated differently by reducing their current balances as at 30 June 2002 and by deducting tax from ongoing employer contributions – refer below for further comment. Similar treatment is given to the Additional Voluntary Contribution Accounts which were introduced into the Scheme from 1 April 2002, in that tax is deducted from additional employer contributions as these are paid, rather than the benefit being reduced at the time of payment. This approach gives more visibility to members and is not inconsistent with the legislation since it only affects a benefit whose availability commenced after the effective date when Scheme's taxation commenced (*ie* 1 July 2000).

Rule 29(7) provides for a slightly smaller benefit reduction where the member contributions are paid post-tax. The purpose of the adjustment is two-fold, *viz*

(a) to reduce slightly the extent of the benefit reductions in order to meet the constraint that the benefit reductions must not lead to a decrease in employer costs; and

(b) to provide a small differential between benefits where there have been post-tax contributions and benefits where there have been pre-tax contributions, in order to make the Scheme cost-neutral for an employer whether member contributions are paid post-tax or pre-tax under a salary sacrifice arrangement.

Rule 30 provides that the crediting rate applied to member accounts will not be reduced on account of tax on investment returns in certain situations. These situations are:-

- all accumulations over the period 1 July 2000 to 30 June 2002, so as to reflect practice to date;
- accumulations for all future years in respect of members who joined the Scheme prior to 1 July 2002, apart from the accumulation of any Additional Voluntary Contributions.

This protection against tax on investment returns only applies up to the level of tax on the basis of taxation law as at 1 July 2000. Also the rules allow for this provision to be modified or ceased by the Superannuation Board, on the advice of the actuary, upon any substantial change to taxation law affecting investment returns.

Rule 31 allows certain benefits to be paid as "untaxed" benefits or as "non-rebateable" pensions. This approach would be used for benefits transferred to the State Scheme and may be appropriate in other circumstances where a member might otherwise be adversely affected by the changes (*eg* a member with significant negative gearing tax losses).

New **Schedule 1A** shows the tax rates to be assumed in the benefit reduction calculations. These rates codify the practice adopted since 1 July 2000 whereby members are assumed to be in a situation where the lowest level of benefit reductions can apply.

Division 5

The amendments to **Division 5** reconstruct Division 5 benefits so that this Division operates as from 1 July 2002 as a normal taxed accumulation scheme. This provides members with a simpler presentation of ultimate benefits than that which must be used in the other Divisions. This approach is possible in Division 5 as there is limited pre 1983 service amongst the Division 5 members.

Rule 11 is amended to ensure that the death benefit for Division 5 is not affected by the reconstruction process. This action is necessary as zero tax is generally payable on a death benefit. Hence there is no tax reduction for death benefits on moving from an untaxed to a taxed arrangement and there is no potential for reducing gross benefits without reducing net benefits. Taxation law provides an "anti-detriment" provision to fund the continuation of the death benefit at its previous level.

A R Archer
Principal, Mercer Human Resource Consulting

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APPENDIX

AMENDMENTS TO THE RULES OF THE ELECTRICITY INDUSTRY SUPERANNUATION SCHEME

REDUCTION OF BENEFITS ON ACCOUNT OF TAXATION

Variations to the Rules made by the Treasurer on 28 June 2002 in accordance with Clause 11 of Schedule 1 of the Electricity Corporations Act 1994 (as inserted by Part 2 of Schedule 3 of the Electricity Corporations (Restructuring and Disposal) Act 1999).

With effect on and from 1 July 2000 Division 1 of the Rules is varied as follows:

1. For the sake of clarity, the definition of "Declared Rate" in Rule 1(1) is amended by inserting immediately before the words "after making allowance for expenses" the words:

   "after taxation on those returns and".

2. The following new Part XV is inserted immediately after Part XIV:

   "PART XV

   ADJUSTMENTS FOR TAXATION

   Taxation Reduction of Benefits

   29. (1) This Rule does not apply to a benefit or part thereof payable under the Rules that is either -

      (a) a lump sum paid as an untaxed benefit in accordance with taxation law, or

      (b) a pension paid as a non-rebateable pension in accordance with taxation law, or

(c) a benefit derived from Additional Voluntary Contributions, or

(d) a benefit payable under Division 5 of these Rules after 1 July 2002.

(2) Notwithstanding any other provision of the Rules, each benefit or part thereof payable under the Rules (other than a benefit or part thereof listed in sub-rule (1) of this Rule) will be reduced in accordance with a formula determined by the Superannuation Board on the advice of the Actuary.

(3) In the case of a benefit or part thereof paid as a lump sum, the formula determined in accordance with sub-rule (2) of this Rule shall be such as to ensure that:

(a) the amount of the reduced benefit or part thereof which would be received after tax, assuming that taxation at the tax rates set out in column B of Schedule 1A of Division 1 of these Rules is applied to the reduced benefit or part thereof;

equals

(b) the amount of the benefit or part thereof prior to its reduction by the formula which would be received after tax, assuming that taxation at the tax rates set out in column C of Schedule 1A is applied to the benefit or part thereof prior to its reduction by the formulae.

(4) In the case of a benefit paid as a pension, the formula determined in accordance with sub-rule (2) of this Rule shall be such as to ensure that:

(a) the amount of the reduced pension which would be received after tax and after taking into account a taxation rebate on pension payments at the rate of 15%;

equals

(b) the amount of the pension prior to its reduction which would be received after tax assuming that it is paid as a non-rebatable pension.

(5) The formula for calculating the amounts received after tax, in accordance with paragraphs (a) and (b) of sub-rule (4) of this Rule, shall take into account the personal income tax scale applicable at the time the pension commences and shall assume that the pensioner receives no taxable income other than the pension.

(6) Where a member contribution in respect of any period after 1 July 2002 (other than an Additional Voluntary Contribution) has been paid by a Member and has not been paid by an employer in accordance with Rule 8A, the reduced benefit determined in accordance with sub-rule (2) of this Rule shall be increased by an amount calculated in accordance with a formula determined by the Superannuation Board on the advice of the Actuary to reflect the excess (if any) of -

(a) 15% of such member contributions after 1 July 2002, accumulated with interest at the Declared Rate,

over

(b) 15% of those member contributions without interest.

Investment Return

30. (1) Notwithstanding any other provision of the Rules, in calculating the investment return of the Scheme assets for a purpose described in sub-rule (2) of this Rule, tax payable in relation to the investments (up to the level of taxation in accordance with taxation law as at 1 July 2000) shall be ignored.

(2) The purposes to which sub-rule (1) of this Rule relates are:

(a) determining the Declared Rates used in Divisions 2, 4 and 5 of the Scheme and the Division 3 Earnings Rates used in Division 3 of the Scheme for both the financial year ending on 30 June 2001 and the financial year ending on 30 June 2002;

(b) determining the Declared Rates used in Divisions 2 and 4 of the Scheme and the Division 3 Earnings Rates used in Division 3 of the Scheme for any period after 1 July 2002, other than for the purpose of accumulating with interest the Additional Voluntary Contributions; and

(c) determining the Declared Rates used in Division 5 of the Scheme for any period after 1 July 2002 for the purpose of calculating the Superannuation Account (as that term is defined in Division 5) in respect of Members who joined Division 5 prior to 1 July 2002.

(3) The application of this Rule may be modified or ceased by the Superannuation Board, on the advice of the actuary, upon any substantial change to the taxation basis affecting the investment returns of the Scheme.

Untaxed Benefits and Non-Rebateable Pensions

31. (1) Where a person is transferred to the State Scheme in accordance with Part 2 of Schedule 1B of the Superannuation Act 1988 any amount paid out of the Scheme assets to the Treasurer shall be treated as an untaxed benefit payment.

(2) The Superannuation Board may determine that:

(a) a lump sum benefit payable under Divisions 2, 3 or 4 of the Rules shall be paid as an untaxed benefit in accordance with taxation law;

and

(b) a pension payable under Divisions 2, 3 or 4 of the Rules shall be paid as a non-rebateable pension in accordance with taxation law.

3. The following new Schedule 1A is inserted immediately after Part XV:

"**Schedule 1A**

ASSUMED TAX RATES
(Rule 29 of Division 1 of the Rules)

Column A Benefit or Part Thereof	Column B Tax Rate	Column C Tax Rate
Lump sum benefit payable as a consequence of the death of a member	0%	0%
Lump sum benefit or part thereof that is payable to a member who is under age 55 and which may be taken in cash:		
- taxed element of the post June 83 component which arose from a taxed rollover into the Scheme	0%	0%
- balance of taxed element of the post June 83 component	21.5%	31.5%
- all other components	0%	0%
Lump sum benefit or part thereof that is payable to a member who is age 55 or over and which may be taken in cash:		
- taxed element of the post June 83 component which arose from a taxed rollover into the Scheme	0%	0%
- balance of taxed element of the post June 83 component	16.5%	31.5%
- all other components	0%	0%
Lump sum benefit or part thereof which must be rolled over to an Approved Benefit Arrangement:		
- taxed element of the post June 83 component which arose from a taxed rollover into the Scheme	0%	0%
- balance of taxed element of the post June 83 component	0%	15%
- all other components	0%	0%"

With effect on and from 1 July 2002 Division 5 of the Rules is varied as follows:

1. Rule 3 is varied by adding immediately after sub-rule (2) the following new sub-rule:

   "(2A) On 30 June 2002 the Superannuation Board will debit to each Member's Superannuation Account the sum of the following amounts –

   (a) 15% of the taxed element of the post June 83 component of the benefit which would have been payable under the Division 5 Rules had the Member ceased employment on 30 June 2000, and

   (b) 15% of the Annual Superannuation Benefit referred to in Rule 4 of these Rules in respect of both the financial year ended 30 June 2001 and the financial year ended 30 June 2002.".

2. Rule 4 is varied by adding to the end of the formula the term:

   "× 0.85".

3. Rule 6A is varied by inserting the following words into sub-rule (2) immediately before the words "and the following amounts must be debited":

   "after making allowance for tax on those contributions and amounts".

4. Rule 11 is amended by deleting paragraph (a) of sub-rule (2) and substituting in its place the following:

   "(a) an amount equal to the amount standing to the credit of the Member's Superannuation Account divided by 0.85;".