

**GUIDANCE NOTE 456 - PREPARATION OF BENEFIT
CERTIFICATES REQUIRED UNDER THE
SUPERANNUATION GUARANTEE (ADMINISTRATION)
ACT 1992**

APPLICATION

Actuaries providing Benefit Certificates under Section 10 of the Superannuation Guarantee (Administration) Act 1992 (the SG Act).

LEGISLATION

This Guidance Note deals with the preparation by actuaries of Benefit Certificates provided to employers under Section 10 of the SG Act.

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CLASSIFICATION

Compliance with the provisions of this Guidance Note is mandatory.

TERMINOLOGY AND DEFINITIONS

"SIS" means the Superannuation Industry (Supervision) Act 1993

"SG Act" means the Superannuation Guarantee (Administration) Act 1992.

"SG Regs" means the Superannuation Guarantee (Administration) Regulations.

"SG Charge" means Superannuation Guarantee Charge.

"NECR" means notional employer contribution rate.

"MRB" means minimum requisite benefit.

"Notional Earnings Base" means the notional earnings base defined in accordance with Sections 13 and 14 of the SG Act.

"Investment Earnings" means the rate of interest determined in accordance with the provisions of SIS and the associated Regulations.

"Regulation" in this Guidance Note means the appropriate regulation under the SG Regs unless the context makes it clear that the SIS Regulations are intended.

1. THE SG ACT

1.1 The purpose of this Guidance Note is to provide guidance to members in relation to the preparation of Benefit Certificates for the purposes of Section 10 of the SG Act.

1.2 Section 10(1) states that: "A benefit certificate is a certificate by an actuary relating to one or more specified defined benefit superannuation schemes and specifying the rate, expressed as a percentage, that is, in the opinion of the actuary, the notional employer contribution rate, in relation to a specified class of employees (being members of the scheme or schemes as the case may be), of an employer who is a contributor under the scheme or schemes (as the case may be) for the benefit of an employee in that class."

1.3 Section 10(2) states that: "The notional employer contribution rate, in relation to a class of employees specified in a benefit certificate relating to one or more defined benefit superannuation schemes, is the contribution rate required to meet the expected long-term cost to an employer who contributes to the scheme or schemes for the benefit of employees in the class, of the minimum benefits accruing in respect of all employees in the class from the date of effect of the benefit certificate onwards."

1.4 Section 10(3) states that a certificate has effect until:

- benefits are changed for any members covered by the certificate
- another certificate is issued

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- a period of five years expires

whichever occurs first.

The Government's intention is that a Benefit Certificate should only expire if minimum requisite benefits are altered, not if other fund benefits are altered. The actuary should interpret Section 10(3) accordingly. The Institute considers it acceptable to provide a Certificate with a term of less than 5 years.

The meaning of the word "expire" is limited in this context. Paragraph 2.5 discusses this issue further.

1.5 Section 10(6) allows regulations to be made regarding the preparation and issue of benefit certificates, and the first such regulations have been promulgated as the Superannuation Guarantee (Administration) Regulations (the SG Regs).

1.6 "Defined benefit superannuation scheme" is defined in the SG Act (Section 6A(1)) as a scheme under which: -

- (a) one or more members of the scheme are entitled, on retirement, to be paid a benefit defined, wholly or in part, by reference to either or both of the following:
 - (i) the amount of the member's annual salary:
 - (A) at the date of the member's retirement; or
 - (B) at a date before retirement; or
 - (C) averaged over a period of employment before retirement;
 - (ii) a specified amount; and
- (b) if the scheme is not a public sector scheme - some or all of the contributions under the scheme (out of which, together with earnings on those contributions, the benefits are to be paid) are not paid into a fund, or

accumulated in a fund, in respect of any individual member but are paid into and accumulated in a fund in the form of an aggregate amount.

The SG Act (Sections 6A and 6B) contains provisions whereby trustees of funds which do not meet the above definition may elect to have the fund treated as if it does meet the definition. These funds are generally known as "deemed defined benefit funds."

For the purposes of the Guidance Note superannuation funds which meet the definition of "defined benefit superannuation scheme" above will be referred to as "defined benefit funds".

1.7 The following points should be noted: -

- Funds falling outside the above definition (ie funds which are neither a genuine defined benefit fund nor a deemed defined benefit fund) do not need a Benefit Certificate.
- Actuaries requested to prepare a Benefit Certificate for a deemed defined benefit fund should comply with Guidance Note 457. Such funds are not explicitly referred to in the remainder of this Guidance Note. However, Guidance Note 457 makes it clear that parts of this Guidance Note apply to the preparation of such Benefit Certificates.
- One member with part of the retirement benefit in defined benefit form is sufficient to render an entire fund a "defined benefit superannuation scheme" for the purposes of the SG Act.
- Once a fund falls within this definition the only way any contributions to, or any benefits from, the fund can be used to offset an employer's SG Charge obligation in a given tax year, is for the benefits to be the subject of a Benefit Certificate. For example members of a defined benefit fund entitled to entirely accumulation -style benefits would need to be the subject of a Benefit

Certificate if the benefits/contributions are to be used to offset the SG Charge.

- A Benefit Certificate can cover more than one defined benefit fund, but cannot include non-defined benefit superannuation funds.
- The Notional Employer Contribution Rate may be any contribution rate, calculated in accordance with the SG Act and this Guidance Note, expressed as a percentage of the Notional Earnings Base. It may be more or less than the rate of employer's SG Charge under the SG Act.
- The Benefit Certificate must clearly identify the classes of employee or member to which the Certificate relates. These need not be defined in the governing rules. The important factor is that at the end of any income tax year, it is possible to determine which class any employee was in at any time during the year.
- It is acceptable to prepare a Benefit Certificate covering more than one employer, relating to a single defined benefit fund.
- A new Benefit Certificate is not required when there is a change in membership composition, even where Section 7 of this Guidance Note is relied on.
- A new Benefit Certificate is not required as a result of a change in actuarial assumptions as part of an actuarial review, even where Section 7 of this Guidance Note is relied on.
- Regulation 4 of the SG Regs requires a Benefit Certificate to be prepared, whether or not Regulation 5 or Regulation 6 is applicable. Benefit Certificates must be prepared in accordance with this Guidance Note, even if Regulation 5 or Regulation 6 applies.

1.8 Where a Benefit Certificate is signed at a date after its effective date, the members who have left the fund since the effective date

should have had their benefits determined as specified in the Benefit Certificate.

2. NOTIONAL EMPLOYER CONTRIBUTION RATES AND MINIMUM REQUISITE BENEFITS

2.1 The Regulations revolve around two basic concepts: -

- (i) The "notional employer contribution rate" (NECR) which is the contribution rate specified in the Benefit Certificate as being appropriate to the "minimum requisite benefits" (MRBs) described on the Certificate for a class of members.
- (ii) The MRB which is the subset of the benefits defined in the governing rules of the fund, which are being valued for the purposes of determining the NECR.

2.2 Each of these concepts is dependent on the other. In practice the most common approach will be to decide what NECR is required, and then to determine the MRBs which are necessary to arrive at the required NECR. However, in some cases the MRB may be the starting point, with the NECR being determined as the end product.

2.3 The MRB must be described in the Benefit Certificate. Regulation 3(2) states that

"A benefit certificate must specify, or identify by reference to the governing rules of each scheme to which the certificate relates, the minimum requisite benefit."

It is not necessary for the governing rules to define the MRB. The Benefit Certificate however, must define the MRB, either by direct description in the Certificate, or by reference to the relevant sections of the governing rules.

It is acceptable for an actuary to prepare a Benefit Certificate which is contingent on appropriate future amendments to the governing rules. The actuary should ensure that the

governing rules at the date of signing the Certificate allow the payment of benefits at least equal to the MRB, either directly or indirectly, for example by way of a discretion available to the Trustee.

The actuary should specify in the Benefit Certificate the mechanism by which the MRBs are expected to be paid, where this may not be clear.

2.4 The description of the MRB should be such that the reader of the Benefit Certificate (and the governing rules where reference is made to these) should be able to determine the MRB for each member covered by the Certificate, for each fund covered by the Certificate, for any mode of exit from the fund at any time during the currency of the Certificate.

2.5 The MRB is subject to the minimum benefit requirements of Part 5 of the SIS Regulations and forms the basis for funding and solvency certification under Part 9 of the SIS Regulations, so that the size of the MRB will have implications for the solvency of the fund in the future.

The actuary should note that the definition of the MRB which accrues during the currency of a particular Benefit Certificate will potentially persist for many years after the expiry of the Benefit Certificate, both for minimum benefit purposes and for solvency purposes. That is, once an MRB has accrued it is covered by the provisions of SIS and cannot be reduced. MRBs should be defined with this in mind and Benefit Certificates should be retained long after their expiry date if they remain relevant.

They will remain relevant unless a replacement Certificate incorporates the MRBs applying from the initial date of the original Certificate.

The actuary should also note that the formula used for determining the amount of preserved benefit relating to the requirement to preserve SG entitlements accruing from 1 July 1994 onwards need not be linked to the MRB formula.

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- 2.6 A Benefit Certificate may cover a period of up to five years, encompassing increases in the requisite SG Charge levels. As a result an actuary may wish to sign a Certificate specifying separate NECRs and/or separate MRBs for separate periods. Such an approach is permitted.
- 2.7 The NECR and MRBs need to be given separately for each class of member or employee covered by the Certificate.
- 2.8 Each member covered by the Certificate must, under the governing rules, be entitled to a benefit at least equal to the MRB, on leaving employment for any reason, at any time during the coverage of the Certificate.
- 2.9 At least the post 30 June 1992 employer-financed component of the MRB, whether in accumulation or defined benefit form, must be based on the Notional Earnings Base, or Section 7 of this Guidance Note must be used. The NECR must be described as a percentage of the Notional Earnings Base.
- 2.10 It is acceptable to prepare a Benefit Certificate which describes the NECR in terms such as "not less than x% of salary". This may be desirable for benefit designs where it is clear by inspection that the benefits are generous enough to satisfy an x% requirement. However, the actuary will still need to define the MRBs precisely in the Benefit Certificate.
- 2.11 It is a Government requirement that it must be impossible for the amount of the accrued MRB to reduce at any time except as a result of salary decreases or negative crediting rates, or as a result of circumstances such as those described in paragraph 6.12.

This principle has very broad application. For example it should apply

- from time to time for a given member
- when a new Benefit Certificate is prepared
- when a member changes category or class of member within a fund
- when a fund's benefit design is restructured.

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- This list is not intended to be all - inclusive, but merely to illustrate the breadth of the requirement. One consequence is that a change of MRB from say accumulation to defined benefit form at a certain age (or length of membership) is not permitted unless it can be demonstrated that no reduction in accrued MRB can occur.
- 2.12 The principle in 2.11 should be applied to the whole of the MRBs where the MRBs are not specifically divided between pre 1 July 1992 and post 30 June 1992 components in the Benefit Certificate.
- 2.13 The only exception to the principles in paragraphs 2.11 and 2.12 is that a single reduction in MRB is permissible on or before 1 July 1993, in view of the timing of the Regulations and this Guidance Note.
- 2.14 Section 6 of this Guidance Note deals with pre 1 July 1992 benefits.
- 2.15 The SG Act places an indexed "cap" (\$83,120 in 1994/95) on the Notional Earnings Base for SG purposes. This "cap" can generally be used -
- in determining the Notional Earnings Base to which the NECR applies
 - in adjusting the contribution base for an accumulation style MRB (see Section 3)
 - in adjusting the amount used as "SAL" in the formulae in paragraph 4.5
 - in determining the MRB where the approach described in Section 7 of this Guidance Note is used.

Note however that where there are member contributions paid out of after tax salary, any part of the MRB which directly relates to such contributions should not make use of the "cap" unless the member contributions were themselves subject to the "cap". Because this requirement was not contained in previous versions of this Guidance Note, the constraint need only apply from the later of 1 July 1995 and the effective date of the first Benefit Certificate issued after that date, where its earlier application would cause difficulties.

3. FULLY ACCUMULATION MRBs

3.1 The approach to be adopted for MRBs of this form is set out in Regulation 5. The NECR should be determined as the employer contribution rate (before any deduction to allow for tax on contributions, expenses or death and disablement costs) which would be required to provide the accumulation.

Regulation 4 states that, where MRBs are in accumulation form, Regulation 5 can be used, with the implication that actuarial certification is not required. However, Section 10 of the Act overrides this implication. The MRBs for all members of a defined benefit fund must be subject to a Benefit Certificate prepared by an actuary in accordance with this Guidance Note. The following procedures apply to MRBs which are fully in accumulation form.

3.2 The intention of the Regulations is that if (say), an NECR of 4% is desired, the benefit payable should be at least: -

- (a) the vested benefit at 30 June 1992 (or the accrued retirement benefit at 30 June 1992 if less), plus
- (b) member contributions from 1 July 1992, plus
- (c) employer contributions of 4% of the Notional Earnings Base, reduced by an allowance for tax on contributions, expenses and death and disablement costs

with Investment Earnings added to all three items.

It is recognised that component (a) is not consistent with the treatment of accumulation funds, where the operation of the SG Act may be such that a greater minimum benefit applies in respect of membership prior to 1 July 1992. Nevertheless, as a minimum the above approach can be followed. See Section 6 for further details.

3.3 The benefits described in the governing rules must result in a benefit at least as great as the MRB, for each mode of exit and for

every possible date of exit, for each member covered by the Benefit Certificate.

3.4 An accumulation style MRB is likely to be used for members of defined benefit funds who have entirely accumulation -style benefits. An accumulation-style MRB may also be appropriate for members whose resignation benefit is in accumulation form, while the retirement benefit is in defined benefit form. In the latter case, to comply with paragraph 2.11, it may be necessary to amend the retirement benefit in the governing rules, so that the retirement benefit is subject to a minimum of the accumulation style MRB defined in the Benefit Certificate.

3.5 The SG Act and Regulations do not place any restriction on the treatment of expenses and death and disablement costs in accumulation funds which are used to meet SG obligations. However, the Government's intention is that the deductions from contributions used to determine the MRB should be determined in a manner which is consistent with the provisions of SIS Regulation 5.02.

This Regulation essentially requires that expenses and death and disablement costs be charged against a member's benefits in such a way that the costs are distributed in a fair and reasonable manner between:-

- (a) all the members of the fund; and
- (b) the various kinds of benefits of each member of the fund

The actuary should note that, while fairness and reasonableness is a matter for a fund's trustees in an accumulation fund, it is a matter for the actuary to consider when preparing a Benefit Certificate.

3.6 MRBs need not be expressed directly in the form of an accumulation of employer contributions, but may be expressed in some other way which bears a close resemblance to such an accumulation. For example the MRB may be in the form of a multiple of member contributions plus Investment Earnings.

In this case the actuary should determine the NECR in a manner consistent with the approach discussed in paragraphs 3.1 to 3.5 above.

3.7 For example, where the member contribution rate is 5% of the Notional Earnings Base, and component (c) [See paragraph 3.2] of the MRB is expressed as equal to 80% of (member contributions from 1 July 1992 plus Investment Earnings) the NECR may be taken as 4%, plus an allowance for tax on contributions and an appropriate share of expenses and death and disablement costs. The principles in paragraph 3.5 must be applied.

3.8 A deduction may be made for tax on employer contributions credited for the purposes of paragraph 3.2(c) regardless of whether or not an employer is actually contributing.

3.9 The approach described in 3.1 to 3.8 above can only be used if the post 30 June 1992 employer-financed component of the MRB is based on a salary definition at least equal to the Notional Earnings Base.

However, where the Notional Earnings Base is something other than ordinary time earnings, it is acceptable to use a Notional Earnings Base at the previous review date for administrative convenience, notwithstanding the method of determining the Notional Earnings Base.

3.10 The SIS Regulations (Regulation 5.01(1)) define "Investment Earnings" in such a way that the earnings on a benchmark portfolio may be used in lieu of the earnings on the fund's assets. Where this approach is adopted, and the MRBs are dependent on the rate of such earnings, the actuary should ensure that:-

(i) the expected return on the benchmark portfolio is likely to be reasonably comparable with the expected return on the fund's assets.

or

(ii) where the return on the benchmark portfolio is expected to be significantly lower than the return in the fund's assets in the long term, the NECR is reduced accordingly.

4. DEFINED BENEFIT MRBs

4.1 Where the MRBs for a member are defined as outlined in this section, the NECR will be evident from the component of the MRB relating to post 30 June 1992 membership.

4.2 For this Section to apply, the MRB on all modes of exit will need to be an amount at least equal to the sum of:

- component (a) relating to pre 1 July 1992 membership; plus
- component (b) relating to post 30 June 1992 membership.

Regulation 6 governs defined benefit-style MRBs. The Government's intention was that the formulae in Regulation 6 and the formulae in this Guidance Note should be identical. However there are some minor differences. Where there is any conflict the actuary should comply with this Guidance Note.

4.3 Component (a) can be in one of the following forms:

- (i) 30 June 1992 Minimum Benefit $\times \frac{\text{Member's Salary at exit}}{\text{Member's Salary at 30 June 1992;}}$
- (ii) 30 June 1992 Minimum Benefit $\times \frac{\text{Final Average Salary at exit}}{\text{Final Average Salary at 30 June 1992;}}$
- (iii) 30 June 1992 Minimum Benefit with interest at the Fund Earning Rate from 1 July 1992 to exit.

where 30 June 1992 Minimum Benefit cannot be less than the lesser of:

- vested benefit at 30 June 1992 determined in accordance with the fund's governing rules at that date; and
- accrued retirement benefit at 30 June 1992 (see Section 6).

4.4 Approach (i), (ii) or (iii) outlined in paragraph 4.3 can be used irrespective of how the 30 June 1992 Minimum Benefit is determined. It is not necessary that one approach be applied to all members of a class. A change of approach is permissible provided the MRB is not reduced for any members. Furthermore, any reasonable mixture of approaches (i), (ii) and (iii) is permissible for an individual

member. The treatment of component (a) is considered further in Section 6 of this Guidance Note.

4.5 Component (b) can be of the form:

- (i) $F \times (MCR/0.85 + NECR) \times SAL \times NM \times DF$; or
- (ii) - member contributions from 1 July 1992 with interest at the Fund Earning Rate; plus
 - $F \times NECR \times SAL \times NM \times DF$; or
- (iii) an accumulation of member and employer contributions as outlined in Section 3.

For the purposes of (i) and (ii) above;

F is 0.0833 for benefits expressed as a multiple of annual salary at date of exit (or review date prior to exit), 0.09 for benefits expressed as a multiple of average salary over three years prior to exit (or three review dates prior to exit), or generally $(0.0833 + 0.0022 \times N)$ for benefits expressed as a multiple of average salary over the N years prior to exit.

MCR is member contribution rate.

NECR is notional employer contribution rate.

SAL is member's annual salary or final average salary at exit on a basis consistent with F and consistent with the determination of the member's Notional Earnings Base. The actuary should note the requirements of paragraph 2.15 where SAL is limited to the "maximum contribution base" as defined in the SG Act, particularly where a formula of type (i) above is used. Where the Notional Earnings Base is something other than ordinary time earnings, in determining SAL it is acceptable to use review date salaries for administrative convenience, notwithstanding the method of determining the Notional Earnings Base.

NM is the number of complete months and fractions of a month from the date on which membership commenced (or 1 July 1992 if later) to the date of exit.

DF is a discount factor, being 1.0 at an exit age of 65, reducing by a simple discount of 1.5% for each complete year (and fractions of a year based on complete months) by which exit precedes age 65, with a minimum discount factor of 0.7 for age at exit of 45 or below. Age 65 applies regardless of the fund's normal retirement date.

NB: For exits in the year to 30 June 1993 it is acceptable to determine NM based on complete months from the date on which membership commenced (or 1 July 1992 if later) to the date of exit (this was the definition of membership in Draft 2, dated 7 December 1992, of this Guidance Note, which was circulated to all members).

- 4.6 If MCR, NECR or the salary averaging period changes, the benefit formula should be adjusted accordingly, with the relevant values of MCR, NECR and F being applied to the appropriate periods of membership.
- 4.7 Use of the approaches outlined in this section is not compulsory. The approach in Section 3 or 5 can be utilised. Alternatively the approach in Section 7 can be used where MRBs are fully or partially in defined benefit form.
- 4.8 Where the approach outlined in this section is adopted, the NECR is simply the NECR included in component (b).

5. MRBs IN MIXED FORM

- 5.1 Mixed form MRBs are possible, provided they conform with the principles described in paragraphs 2.11 and 2.12.

For example an MRB of the form: -

(Member contributions with interest) plus
a percentage of

(A discounted accrued retirement benefit less member
contributions with interest)

is permitted.

- 5.2 In these cases the NECR relating to the accumulation style benefit should be determined in a manner consistent with Section 3 of this Guidance Note. The NECR relating to the defined benefit style benefit should be determined in a manner consistent with Section 4 or 7 of this Guidance Note.
- 5.3 Where it is not clear how Sections 3 and 4 apply to a particular design, Section 7 of this Guidance Note must be used.

6. PRE 1 JULY 1992 BENEFITS

- 6.1 The Government's reasoning behind the treatment of pre 1 July 1992 benefits is to prohibit any significant use of benefits accrued before 1 July 1992 to meet the cost of providing benefits which are being used to meet the employer's liability to SG Charge. The basic starting point is the vested benefit at 30 June 1992. It is recognised that use of the vested benefit does not fully address this issue, but it was felt by the Government to be a practical solution which prevents most of the potential abuses.
- 6.2 The Government's reason for using the lesser of the vested benefit and the accrued benefit as the pre 1 July 1992 minimum benefit, as specified in the Regulations, is to cover the situation of a member accruing a vested benefit of say seven times final average salary some years before normal retirement date, with no further benefit accruing once seven times final average salary is reached. The Government's intention is to avoid forcing the use of a pre -1 July 1992 minimum benefit which is more generous than linear progression of vesting would provide.

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- 6.3 However, there is potential for this provision to be misused in other situations, and as a result it is necessary to constrain the method of calculation of the accrued benefit in this Guidance Note, to ensure that the resulting accrued benefit amount is not unduly small. Actuaries should comply with this Guidance Note where it is inconsistent with Professional Standard No 402 or where it covers matters not dealt with in that Standard. Otherwise actuaries should comply with that Standard.
- 6.4 Where the normal retirement benefit is a fixed multiple of salary, or final average salary, or the normal retirement benefit is a fixed dollar amount, or is calculated by a formula based on a benefit accrual period, the accrued benefit should normally be calculated as:-

$$\frac{\text{benefit accrual period to 30 June 1992}}{\text{benefit accrual period to normal retirement date}} \times \text{normal retirement benefit}$$

Where the benefit is salary related the normal retirement benefit should be calculated using current salary or final average salary in a manner consistent with the calculation which would apply at normal retirement.

Where the fund does not have a specified normal retirement date, age 65 should normally be used instead, where retirement is possible at this age. If retirement is compulsory before age 65, the latest possible date of retirement should be used.

Alternatively, a retirement age established clearly by past practice may be used.

The benefit accrual period should be calculated in complete months, or more accurately.

- 6.5 The approach in paragraph 6.4 above should be used unless the actuary has clear grounds for believing the result to be inappropriate. An example might be where significantly different accrual rates apply for different periods.

If the actuary believes that the approach in paragraph 6.4 is inappropriate, the accrued benefit may alternatively be calculated by determining the benefit accrued on the formula which would apply if normal retirement were available at 30

June 1992, using salary or final average salary (in a manner consistent with the calculation of the normal retirement benefit) as at 30 June 1992.

6.6 It is acceptable to use salaries at fund review dates in the calculation of the accrued benefit, even though the normal retirement benefit rule may specify some other form of calculation. For example, if the normal retirement benefit is based on final average salary over the 36 months prior to normal retirement date, it is acceptable to use salaries at the three review dates on or preceding 30 June 1992 in calculating the accrued benefit.

6.7 There may be cases where application of paragraphs 6.4 to 6.6 above is not possible, or where the procedures described give an unreasonably low value for the accrued benefit.

If this is the case, the actuary may determine how to calculate the accrued benefit. In these circumstances, the method of determination of the accrued benefit should be described fully in the Benefit Certificate.

6.8 In determining the vested benefit at 30 June 1992, it is not necessary to assume that the employer or the trustees will exercise certain discretions in a member's favour. For example, where a member at 30 June 1992 is entitled on exit to either (i) a higher benefit if the employer exercises a discretion to allow early retirement or (ii) a lower benefit if this discretion is not exercised, either benefit is acceptable as the vested benefit at 30 June 1992.

6.9 Where a higher level of benefit is subject to a certain period of notice being provided by a member, in determining the vested benefit it should be assumed that such notice has been given. For example, where an early retirement benefit is payable on three months' notice being given by the member, and such a benefit is greater than the resignation benefit which would otherwise be payable, the vested benefit at 30 June 1992 should be taken as the early retirement benefit, provided this would have been payable at 30 June 1992 had the member given the required notice.

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- 6.10 Where the benefit at 30 June 1992 is subsequently updated in line with salary increases, rather than by addition of interest, it is acceptable to use salaries (or average salaries) at fund review dates, provided a consistent approach is applied to both salaries (or sets of average salaries) in the updating process.
- 6.11 Where the member has a choice of benefit on exit, for example a cash lump sum or an alternative deferred lump sum, any of the benefits available may be used in determining the vested benefit at 30 June 1992.
- 6.12 If the member leaves in circumstances where the member would not have been entitled at 30 June 1992 to the benefit which has been taken to be the vested benefit at 30 June 1992 (the circumstances might include fraud, insolvency, not providing the required period of notice etc), then the 30 June 1992 vested benefit in the MRB formula may be replaced by the benefit which would have been payable at 30 June 1992 had the member left in similar circumstances to those in which the member is actually leaving, provided that the resulting MRB is not less than is required to comply with SIS Regulation 13.16.
- 6.13 Where the vested benefit or accrued benefit is in the form of a deferred benefit, and it is necessary to place a lump sum value on the deferred benefit, the actuary should use assumptions to value the benefit which are consistent with those used, or those which would be used, in an actuarial valuation of the fund.
- 6.14 Paragraphs 6.1 to 6.13 were drafted in the context of determination of the initial MRB at 1 July 1992. There will be circumstances where it is necessary to determine an initial MRB at some other date. An example would be a defined benefit fund used for SG purposes for the first time from 1 July 1995. In such cases an initial MRB should be determined using the principles in paragraphs 6.1 to 6.14 but with references to 30 June 1992 being replaced by the relevant date.

7. NON-STANDARD APPROACH

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- 7.1 Where MRBs are fully or partially in defined benefit form, it is not compulsory to use the standard approaches described in Sections 4, 5 and 6 of this Guidance Note. The alternative procedure described below may be used instead.
- 7.2 The NECR and the MRBs should satisfy the following testing procedure:-
- (i) The defined benefit component of the MRBs should never produce a future service benefit for any individual which is less than 80% of the benefit which one of the standard defined benefit formulae in paragraph 4.5(i) and (ii) would provide. This test should be satisfied for all potential new entrants to and all existing members of a class.
 - (ii)
 - (a) Using appropriate actuarial assumptions, determine PV, which equals the present value of the future service component of the defined benefit element of the MRBs, less the present value of future member contributions for existing members in the class. In determining PV, all future service defined benefit MRBs should be restricted to an upper limit of 125% of the amount which one of the standard defined benefit formulae in Section 4 would provide.
 - (b) Using the same actuarial assumptions, determine PVF, which equals the present value of the future service component of the defined benefit element of the MRBs which would apply using one of the standard defined benefit formulae in Section 4, for existing members in the class less the present value of future member contributions.
 - (c) For the Benefit Certificate to be valid, PV cannot be less than PVF.

Throughout this testing procedure, the choice of standard option i.e. paragraph 4.5(i) or (ii) should

be consistent for all members in a class, and should be consistently used in parts (i), (ii)(a) and (ii)(b) above.

- 7.3 In carrying out the test under paragraph 7.2(ii) the actuary should normally use assumptions consistent with those used for the last actuarial valuation, where one has been carried out. However, the assumptions should be reasonable having regard to expected experience for the class of members concerned. Death and disablement decrements should be ignored, or the benefit set equal to the resignation or retirement benefit. This is because such decrements have been implicitly allowed for when arriving at the standard formulae. No account should be taken of future new entrants.
- 7.4 In paragraph 7.2 the benefits to be tested must be payable of right, and not subject to the exercise of a discretion or consent by the employer or trustees.
- 7.5 Accumulation style components of MRBs may not be included in this testing procedure. Where the MRB is such that it is not possible to apply the testing procedure in Section 7, or to apply one of the standard approaches in Section 3, 4 or 5, the form of the MRB must be changed, if the actuary is to provide a Benefit Certificate in accordance with this Guidance Note.
- 7.6 The membership to be used in the testing procedure may be the membership at any date from the date of the last actuarial review to the date of signing the certificate. "Future service" should apply from the effective date of the Benefit Certificate.

8. MISCELLANEOUS ISSUES

- 8.1 Pension benefits are not explicitly covered by the Regulations. In a genuine pension scheme i.e. one where benefits have been taken as pensions in practice, the actual pensions payable to the member including reversions should be valued, as in Section 7 above. Only pensions payable to the member as of right, including reversions, should be valued. Entitlements to pension increases may be valued, but discretionary pension increases should not be taken into account.

However, where in practice pensions are normally commuted to lump sums, commutation factors which are consistent with those used for commuting pensions should be used instead, whether or not these factors are guaranteed.

- 8.2 Where benefits are not funded or an election is made under Section 274(7) of the Income Tax Assessment Act, an appropriate adjustment to the standard formula in Section 4 should be made to allow for the differential tax treatment.
- 8.3 If any improvements to benefits are made after 30 June 1992 which have the effect of retrospectively increasing benefits, the pre 1 July 1992 component of the MRB need not be increased in line with the benefit improvement.
- 8.4 Deferred benefits payable from a future date should be discounted to the date of exit using suitable actuarial assumptions, where the actuary wishes to express the MRB in a lump sum form.
- 8.5 Where there are multiple forms of benefit available to a member on exit, at the member's option, each form of benefit must be at least equal to the MRB where there is no immediate lump sum option.

Where one of the options is an immediate lump sum, it is sufficient that the immediate lump sum is at least equal to the MRB, unless in practice a significant proportion of members do not take the immediate lump sum, in which case all options must be at least equal to the MRB.

- 8.6 When determining the MRBs, the actuary should consider all the possible circumstances in which benefits may be paid from the fund in practice. Where relevant the actuary should allow for:-
- Benefits which may be paid in addition to the normal fund benefits. These may include additional benefits in respect of voluntary member contributions, additional employer-financed accumulations, benefits granted in respect of past or future transfers into the fund etc.
 - The treatment of fund transfers should be consistent with the requirements of Part 5 of the SIS Regulations.

Alternatively it is acceptable to deal with bulk transfers by transferring the former fund's MRB formula into the current fund, provided the actuary is satisfied such an approach is reasonable in the circumstances.

- Changes in membership status, such as leave of absence, changes to contribution or accrual rates, category transfers, changes between full and part-time status etc.
- The treatment of MRBs beyond normal retirement date
- Calculation of FAS where the membership period is less than the salary averaging period
- The treatment of salary reductions

- 8.7 The actuary should consider the effect of any past or future changes to associated employers or to the structure of the fund on the Notional Earnings Base applying to each class of members covered by the Certificate. For example if a new associated employer is admitted to the fund, or there is a bulk transfer of members into the fund, a Notional Earnings Base definition which had previously been relevant to all members covered by the Benefit Certificate may no longer be applicable for some members.

The actuary should consider incorporating sufficient flexibility into the MRB and NECR definitions to accommodate such changes, or ensure the Benefit Certificate is replaced where necessary.

- 8.8 All contributions which are made from pre-tax salary (whether by salary sacrifice or not) are employer contributions for the purposes of the SG Act and this Guidance Note ie the employer is entitled to use them to offset its SG Charge obligations if the benefits in respect of those contributions are treated as part of the employer-financed component of the MRB. While such treatment is legal in all cases, there may be circumstances in which the employer and/or the trustees prefer to treat such contributions as if they were member contributions for MRB purposes. In such cases the actuary may treat the contributions as if they were member contributions for the purpose of this Guidance Note, but

ignoring the adjustment for contribution tax which normally applies to member contributions (see section 4.5).

- 8.9 MRBs do not need to be in the form of an immediate lump sum. They can take the form of an immediate or deferred pension, or a deferred lump sum. However Section 7 of this Guidance Note must be used unless:
- a) the MRB is a deferred lump sum, increasing with Investment Earnings or an earnings index during deferment; or
 - b) the MRB is in the form of an immediate pension commutable using factors guaranteed in the fund's governing rules; or
 - c) the MRB is in the form of a deferred pension, increasing in deferment as described in a) above and commutable in a manner consistent with b) above.

Note that deferred benefits increased in line with a price index must be subject to the approach in Section 7.

9. INFORMATION TO BE INCLUDED IN BENEFIT CERTIFICATES

- 9.1 The Benefit Certificate must include: -
- (a) The name of the employer/s requesting the Certificate, or if the Trustee of the superannuation fund has requested the Certificate on behalf of the employer/s, the name of the Trustee.
 - (b) The name of each superannuation fund to which the NECR relates.
 - (c) A description of each class of members covered by the Certificate.
 - (d) The NECR for each class of members covered by the Certificate.

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- (e) A statement that each NECR has been calculated in accordance with the SG Regs and these Guidance Notes.

The actuary's attention is drawn to Regulation 4 and the statement required therein. The Institute considers that the required statement may be made in the case of every Benefit Certificate which complies with this Guidance Note, and the Benefit Certificate should include the required statement.

- (f) A description of the MRBs for each class of members covered by the Certificate, either directly or by reference to the governing rules.
- (g) A description of the approach adopted when allowing for death and disablement costs and expenses, where the MRB has an accumulation component.
- (h) Where the procedure in Section 7 of this Guidance Note is adopted, a description of the assumptions used, together with a description of the method of apportioning benefits between past and future membership.
- (i) The method of determining the accrued benefit at 30 June 1992, where paragraph 6.7 of this Guidance Note is relied on.
- (j) The date on which the Certificate takes effect.
- (k) The date beyond which the Certificate will cease to have effect in the opinion of the actuary.
- (l) The name, address and qualifications of the actuary.
- (m) The date of signing the Certificate.

10. REPLACEMENT OF BENEFIT CERTIFICATES

- 10.1 Section 2.11 states the key principle that "it is a Government requirement that it must be impossible for the amount of the accrued MRB to reduce at any time...". This principle should be borne in mind whenever a Benefit Certificate is replaced.
- 10.2 It is acceptable at the point of change of an MRB formula to determine the dollar amount of the accrued MRB, and to use this as the base for the future MRB. Alternatively the dollar amount may be converted to a multiple of SAL (or other relevant salary definition), with the multiple being used as the base for the future MRB formula. Another option is to retain the existing formula, or some alternative which is guaranteed to give an equal or better result, in respect of membership prior to the change.
- 10.3 Where a Benefit Certificate contains a typographical error the Benefit Certificate can be replaced at any time with a corrected Benefit Certificate with the same effective date.
- 10.4 A Benefit Certificate can be retrospectively replaced with a new Certificate having the same effective date as the old one where the change is such that no part of any MRB accruing prior to the effective date of the replacement Certificate is reduced for any member covered by the Certificate (ie. Section 2.11 is complied with). Members who have left the fund since the effective date should have their MRB determined as specified in the new Benefit Certificate.

Retrospective replacement of a Benefit Certificate with a reduced MRB is permitted provided the actual benefit payable at the date of replacing the Benefit Certificate (or any earlier date) does not reduce and provided the replacement is in accordance with the provisions of the trust deed and the SIS Regulations (particularly Regulation 13.16).

- 10.5 A common circumstance which arises in practice is that after the Benefit Certificate is issued it is determined that contributions that could be counted to offset the Superannuation Guarantee charge have been paid to another complying fund, eg. 3%

contribution to an industry fund. This is a specific example of the more general case where the actuary wants to retrospectively reduce MRBs for some valid reason.

Where the MRB has been reported to members they will need to be advised of any reduction in MRB.

Where a retrospective reduction in the MRB would reduce the actual benefit payable at the date of replacing the Benefit Certificate the replacement of the Certificate must be referred to the Tax Office for approval.

Where the MRB has been defined within the governing rules any retrospective reduction in MRB would generally require approval from the ISC and/or all the fund members.

- 10.6 Any other cases where retrospective reduction of the MRB applies requires Tax Office approval.

11. CODE OF CONDUCT

- 11.1 This Guidance Note has been prepared on the assumption that the actuary undertaking the work is familiar with the operations of the superannuation fund through other work done for the fund. In practice, this may not be so, in which case the actuary should have regard to the Code of Conduct particularly Guidance Notes B9 and B10.

END OF GUIDANCE NOTE 456