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Ms Monika Binder
Productivity Commission
PO Box 80
BELCONNEN ACT 2616

Dear Ms Binder

PORTABILITY OF BENEFITS - GOVERNMENT EMPLOYEES SUPERANNUATION BOARD

Thank you for your e-mail of 2 August 2001 to Adrian Warner, and the opportunity to comment on the concerns raised in relation to the portability of benefits in the Gold State Super scheme.

I have attached for your reference an explanatory note in relation to the design and treatment of benefits in the Gold State Super scheme.

In relation to the specific issues canvassed in your e-mail,

- The rules governing the treatment of benefits and the general requirement requiring preservation of benefits until age 55 are a result of the unfunded nature of the scheme. The Western Australian Government's policy in regard to this is reflected in the provisions of the *State Superannuation Act 2000* and the *State Superannuation Regulations 2001*. This legislation replaces the *Government Employees Superannuation Act 1987*, referred to in the correspondence from Mr Cox.

- Where the GESB's benefits are fully funded, vested benefits are fully portable. Recent borrowing has allowed full funding of fund benefits in the GESB's accumulation scheme, West State Super. The Government, however, is not in a position to extend such an arrangement to all Gold State Super members, as such a change would bring forward costs to the Government of up to $2,134 million. The Heads of Government Agreement acknowledges that there are substantial differences between public sector schemes and those in the private sector. In respect of portability, the Heads of Government Agreement recognises that portability may be restricted due to the benefit design of a fund.

- The unfunded nature of the Gold State Super scheme means that the State meets the majority of its funding obligations only at the time benefits become payable on or after age 55. At this stage this is not considered feasible to bring forward the cost to government.

I hope this information is of some assistance. If you have any further queries, please contact me on (08) 9263 4289.

Yours sincerely

SEAN DAVID
POLICY OFFICER

17 October 2001

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GOLD STATE SUPER – INDEXATION AND PORTABILITY OF DEFERRED BENEFITS

Rules on Preservation of Gold State Super Deferred Benefits

With limited exceptions, all members of Gold State Super (the defined benefit, lump sum contributory scheme) who cease employment in the State public sector prior to age 55 years are required to preserve their accrued benefit in the Government Employees Superannuation (GES) Fund until age 55 years. These benefits are indexed at the rate of CPI + 1% per annum and generally become payable at age 55 years. This general rule has been in place since the scheme was established in 1987.

The exceptions to the rule are:

1. Employees who have accepted a redundancy package or transferred to the private sector since 30 December 1995, or;
2. Where a public sector agency operates on a commercial basis, has been given permission to set up its own corporate superannuation arrangements, and the member elects to transfer to that fund.

In these circumstances members are able to transfer the current value of their Gold State Super benefits out of the GES Fund. This initiative was introduced by the then State Government to facilitate its public sector reform program and provide an additional incentive for affected persons to make the transition from a public sector to private sector environment.

Where members choose to transfer their benefit to another superannuation fund the nominal benefit is discounted at the rate of 1.75% per year remaining to age 55 years to reflect the current value of the benefit. This discount has been determined by the GES Board based on specialist actuarial advice and is applied to the value of a person's contributory service component of their preserved benefit. No discount applies to the other components of the benefit.

Rationale for CPI + 1% Indexation Rate

The indexation rate of CPI + 1% is an integral part of the overall Gold State Super scheme design. In the context of the scheme design, CPI + 1% is not a substitute for investment return but rather is the assumed annual rate of salary increase. The level of benefits and contribution rates for members and employers are linked to the level of the indexation rate. That is, in return for contributions of 5% and 12% of a member's current salary by member and employer respectively, the State guarantees to pay a benefit on retirement of 20 percent of the member's average final salary for each year of membership service.

For members who remain public sector employees until retirement final salary can be calculated easily. However, for members who exit the scheme prior to retirement final salary is defined to be their average final salary when they ceased employment indexed at the rate of CPI + 1% per year until the benefit is paid.

The level of benefits in Gold State Super and the contribution rates for members and employers are based on the principle that deferred benefits are preserved in the GES Fund until at least age 55 years and indexed at CPI + 1% per year. In order to provide a rate higher than CPI + 1% either the level of member and employer contributions would need to increase or the rate of accrual of benefits would have to decrease. Neither of these alternatives is considered feasible.

In times of low inflation, the indexation rate of CPI + 1% per year may not appear to compare favourably with crediting rates in accumulation schemes. However, this rate does provide for a real increase in the value of deferred benefits over time and importantly, is guaranteed by the Government. It also needs to be viewed in the context of the overall scheme design, which offers a high rate of accrual of benefits, no administration fees and a generous level of insurance cover at no additional cost to the member during their period of employment.

Defined Benefit Schemes vs Accumulation Schemes

It is not valid to compare the CPI + 1% indexation factor in a defined benefit scheme like Gold State Super against the crediting rates in accumulation schemes that are linked to a fund's actual performance.

Defined benefit schemes offer a guaranteed retirement benefit, with the employer bearing all of the investment risk. The nominal value of a defined benefit multiple at any point prior to the payment date does not necessarily equal the actual value of the member's entitlement at that time. This is why transferred benefits are subject to a discount.

In comparison, an accumulation scheme benefit consists of member and/or employer contributions plus net investment earnings on these contributions, less administration and insurance costs. Therefore, the actual value of an accumulation scheme benefit is always the nominal value recorded on an ongoing basis in the member's account.

Portability of Gold State Super Benefits

The general restriction on rollovers prior to age 55 years is due principally to the funding arrangements of Gold State Super, which is largely unfunded. That is, the State meets the majority of its funding obligations only at the time benefits become payable, generally on or after age 55 years.

The Government is not in a position to extend the existing limited rollover provisions to all current and former Gold State Super members as such a change would bring forward costs to the Government of up to $200 million and is therefore not considered feasible.

GOVERNMENT EMPLOYEES SUPERANNUATION BOARD
May 2001