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AUSTRALIA

The PSS BOARD

Public Sector Superannuation scheme

Annual Report 1996-97

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The PSS Board

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Note: All contribution, benefit and membership and exit statistics are based on events related to the annual reporting period as reflected in the records of the Commissioner for Superannuation at the time these statistics were compiled. As such, the statistics may vary from the records of these events as recorded by departments and authorities. Where historical statistics are quoted, these may vary from previously published statistics due to the application of retrospective adjustments that are now reflected in this report.

Letter of **Transmittal**

The Hon. John Fahey, MP
Minister for Finance
Parliament House
Canberra ACT 2600

Dear Minister

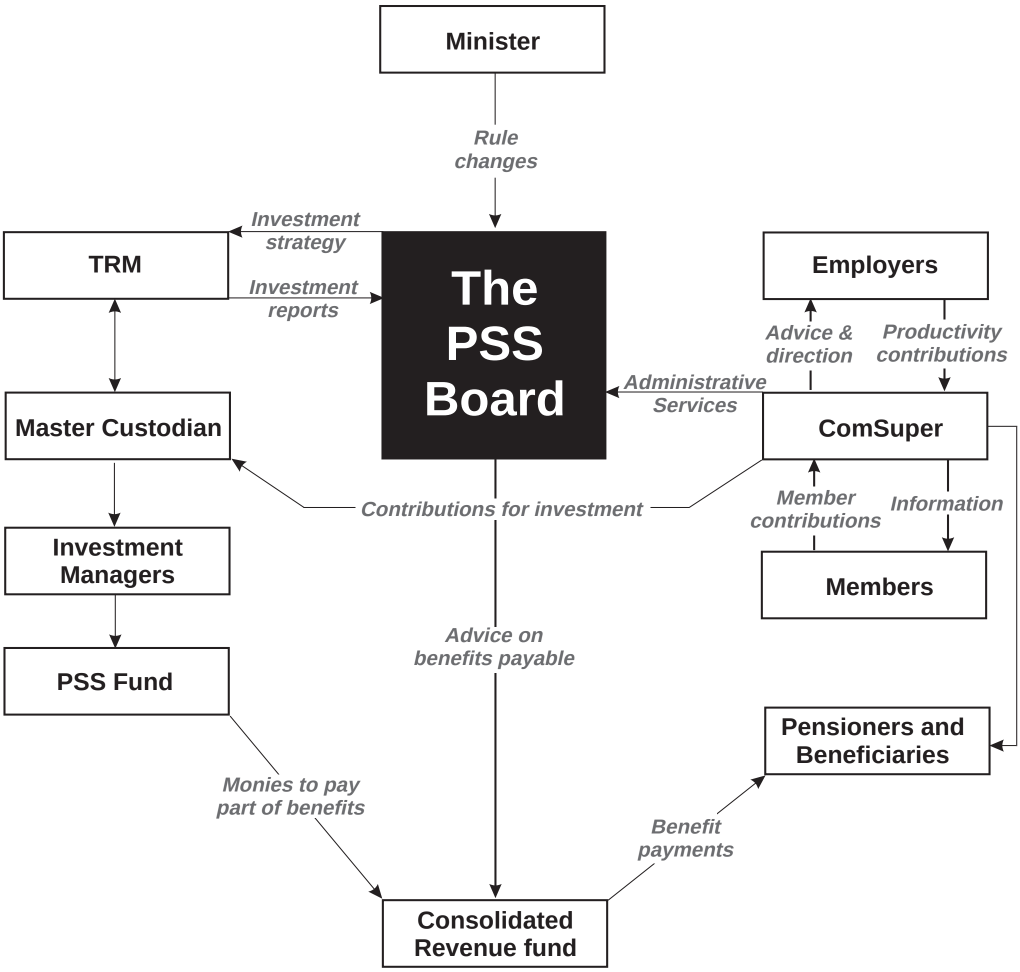
In accordance with section 28 of the *Superannuation Act 1990*, the PSS Board is pleased to present to you the annual report on its operations during 1996–97. The Report details the Board's activities in respect of the administration of the Public Sector Superannuation scheme and includes audited financial statements in respect of the management of the PSS Fund during the year ended 30 June 1997.

(signed)

Ron Brown
Chairperson
PSS Board

10 October 1997

There are a considerable number of entities involved in scheme administration and fund investment.
This chart shows the more significant interrelationships.



The PSS Board
Its responsibilities and administrative arrangements

Year in brief

During 1996–97, in addition to administration of the Fund and the Scheme, the Board's attention was primarily focused on:

- issues arising from the sale of Commonwealth Funds Management (CFM) and Total Risk Management (TRM);
- establishing arrangements to assume the trusteeship role in relation to pooled investment vehicles formerly held by CFM;
- the development of a business plan for the Board;
- establishing improved reporting arrangements to enable the Board to more effectively monitor the performance of the scheme administrator;
- reviewing the strategic asset allocation adopted by the Board in April 1996 (this review resulted in a net increase in the level of investment return in Australian shares); and
- developing a cash flow strategy to meet redundancy payouts during a period of significant staffing reduction in the public service.

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Summary of events

In 1996–97 major events included the sale of CFM and TRM, the 'Choice' campaign, an increased level of public sector redundancies and a new investment focus.

The PSS Board implemented a new strategic asset allocation. As a result of this move, the PSS Fund performed very well.

The implementation of ComSAS resulted in overcoming accounting difficulties relating to separation of CSS and PSS funds.

Return on investments

The after-tax and fees return on investments achieved by the Fund in 1996–97 was a very creditable 17.82 per cent, thanks mainly to a timely increase in domestic and overseas shares. That move was made as a result of our decision to implement a more aggressive investment policy.

In line with that decision we increased the Fund's exposure to international shares from 25 per cent to 40 per cent and its exposure to domestic shares from 28 per cent to 33 per cent. At the same time, we reduced the Fund's holdings in fixed-interest and indexed bonds. As a result the Fund was well placed to take advantage of the excellent returns achieved by all major share markets during the last quarter of 1996–97.

Public sector redundancies

During 1996–97, 8322 PSS members left the scheme as a result of APS-wide redundancy programs.

Through careful forward planning we were able to manage the cash flow needs of those payments in an orderly manner to meet our commitments to exiting members without impacting on our investment performance.

With the possibility of continuing large-scale redundancy programs next year, we will continue to follow strategies aimed at managing the cash-flow consequences of redundancy payments.

Sale of CFM and TRM

Prior to 30 June 1995 Commonwealth Funds Management Ltd (CFM) held an exclusive (legislatively imposed) mandate for the investment of the PSS Fund. However, with effect from 1 July 1995 this exclusive mandate expired, and during 1995–96 the Board implemented an innovative approach to the management and investment of the Fund. This involved a move away from the more traditional balanced fund approach to a modular fund structure wherein each asset class consists of both core and specialist components. The core components are passively-managed (with no active stock selection) and aim to capture market returns for the particular asset class. The specialist components allow for controlled diversity through a range of active investment managers, with complementary management styles, who focus on different market segments.

In implementing this new investment approach, significant elements of funds under management were progressively moved away from CFM to some 20 or so active specialist managers. Further work to review the management arrangements for core components of the Fund was under way at the time of the announcement by the government of its intention to sell CFM and its subsidiary company Total Risk Management Pty Ltd (TRM), but the Board agreed to delay that further work until sales negotiations had been completed.

In December 1996 the government announced that CFM had been sold to Commonwealth Financial Services (CFS—the investment arm of the Commonwealth Bank) and that TRM had been sold separately to the actuarial firm Towers Perrin.

CFS currently has responsibility for the management of most of the core portfolios (representing approximately 70 per cent of the total fund) but the Board has agreed a timetable for the review of the core mandates which should see that process finalised by the end of 1997.

Key personnel within TRM have been retained by the new owner and as a result TRM continues to act as the Board's primary adviser on investment matters.

Investment strategy

In April 1996, with the assistance and advice of TRM, the Board adopted a new strategic asset allocation which was implemented during the early part of the 1996–97 financial year. The combination of assets which best met the Fund's investment objectives included a large proportion of shares, both Australian and overseas, together with smaller proportions of property, bonds and other asset classes, including alternative investments.

The greatest proportion of the Fund is invested in overseas shares, while more than 30 per cent is in Australian shares. The move to increase the Fund's exposure to international shares had regard to the inherent limits on return opportunities through investment solely in the Australian equities market. The wider opportunity provided by investing in the much larger world markets also takes into account that there are some growth industry sectors not represented in Australian shares. The Board's research indicates that the strategic asset weightings now adopted will position the Fund to capture higher real rates of return for the Fund and its members over the longer term.

Investments in overseas shares

During the course of the year the Board received a number of expressions of concern regarding the level of offshore investment by the Fund. Those concerns were mostly based on the assumption that concentration on investment in domestic shares would increase employment opportunity in Australia.

The Board does not believe that employment generation should or could (given the objectives of the Fund and the requirement for Trustees to act in the financial interests of its members) be an objective of the Fund. However, we have given some thought to the effect of investment decisions on employment generation.

From the evidence, it appears that increased trading in a share market does not necessarily lead to increased employment opportunity; rather it leads to a change in the value of the share traded. More important factors affecting employment include the operations of the capital, product and labour markets.

Recent research has shown that the injection of equity capital for new development ventures or infrastructure projects has the potential to impact on job creation. The research shows that this type of investment has been a major factor in the creation of new jobs in the United States for the past decade. It has been an important part of the process which has seen the US economy move away from manufacturing and towards service industries.

The same trend has been observed in the Australian economy. While the domestic opportunities for investments in new development ventures or infrastructure projects are modest, they are growing. The Board has already made a number of such investments and continues to place a high priority on investigating new opportunities as they arise.

Crediting rate

As a result of the very satisfactory 1996–97 investment performance, the Board was able to declare an annual crediting rate of 14 per cent. This result exceeds the annual inflation rate by 13.7 per cent. When taken with the returns for recent years, the Board has more than met its objective of achieving a real return on members' accumulated contributions of at least three per cent above the rate of inflation.

Development of Business Plan

During a review of administrative arrangements conducted in the 1995–96 financial year, the Board decided to implement a number of new initiatives. One of these was the development of a fully integrated business plan. The Board embarked on this process during the 1996–97 financial year and considerable progress has been achieved.

The Board engaged Mr Paul Cheever of PlanPerform Pty Ltd initially to assist with the development of the structure of the business plan. This arrangement was then extended for a twelve month period (commencing on 6 March 1997) to assist the Board in the further development of the business plan, in implementation of the actions set out in that plan, in the review of the Board's relationships with its administrator and investment adviser, and in the provision of advice on general policy matters.

As one of the initiatives flowing from the business plan, the Board has established a Communications Sub-Committee. Its task is to oversee the Board's communications strategy with members.

Choice campaign

As a result of representations by the ACTU, the previous government decided to give eligible CSS members a second chance to elect to transfer to the PSS (eligible CSS members had previously been given the opportunity to transfer in 1990–91 when the PSS was first introduced).

The six-month ‘Choice’ period opened on 1 March 1996 and closed on 2 September 1996.

During the campaign, 8690 eligible CSS members transferred to the PSS. This represents about 13 per cent of the eligible CSS population.

No Audit qualification

The Board’s Audit Committee participated in the development of ComSuper’s forward internal audit program for 1997–98 and monitored the progress of audits undertaken in the course of the 1996–97 program.

In previous annual reports, the Board has reported on the major project being undertaken to redevelop the computer systems used by ComSuper to administer the PSS scheme. A major aim of the project was to overcome accounting shortcomings, which had in the past led to the Board having its financial statements qualified by the Auditor-General. Following successful implementation of the first phase of the new computer system, it is pleasing to be able to report that for the first time since 1992–93, the Board’s financial statements have been completed without audit qualification.

SIS standards

The PSS scheme remained a complying Fund under the *Superannuation Industry (Supervision) Act 1993* (SIS) and so continues to be eligible for concessional tax treatment.

Thank you

I would like to thank the Trustees for their hard work and cooperation throughout the year, and in particular I thank those trustees who contributed to the working of the Board's sub-committees, the Audit Committee, the Reconsideration Advisory Committee and the newly formed Communications Committee.

Two of our Trustees left the Board during the year. Ken Searson resigned on 14 February 1997 and Michael Hutchinson's appointment came to an end on 30 June 1997. Each brought particular skills and experience to the Board's work, which was greatly valued, and I here record the thanks of the Board as a whole to each of them. Mr Searson has been replaced by Mr Peter Reynolds while Mr Hutchinson's replacement, Mr Graham Kelly, was formally appointed to the Board on 25 July 1997. I welcome both of these new Trustees to the Board.

Ron Brown
Chairperson
PSS Board

Fund investment

ASSET ALLOCATION	1995–96		1996–97	
Sector	$m	%	$m	%
Property	394.8	18.6	371.2	15.2
Australian equities	593.9	28.0	763.9	31.2
International equities	850.8	40.2	1 022.6	41.8
Australian Fixed-interest [1]	278.8	13.2	290.3	11.8
Total	**2 118.3**	**100.0**	**2 448.0** [2]	**100.0**

INVESTMENT PERFORMANCE [3]	1995–96		1996–97	
Sector	Benchmark %	Fund %	Benchmark %	Fund %
Property	6.3	4.6	4.8	0.4
Australian equities	13.4	12.9	24.6	26.6
International equities	5.7	4.6	24.8	23.1
Australian Fixed-interest	8.0	9.0	12.6	11.1
Return on investment	**8.5**	**8.5**	**19.0**	**18.0**
ANNUAL CREDITING RATE [4]	7.2 %		14.0 %	

Notes

1 Includes cash and indexed bonds.

2 This represents the funds under management at 30 June 1997, and will differ from the investments shown in the financial statements because of necessary accounting adjustments.

3 Performance figures are after tax and fees.

4 Annual crediting rates differ from earning rates because of various adjustments, including transfers to and from the Reserve Account (see also *Note on calculations* on page 27).

Scheme membership

CONTRIBUTORS AT 30 JUNE	1996	1997	plus/(minus) %
Male	53 574	50 271	(6.2)
Female	67 200	63 852	(4.9)
Total	**120 774**	**114 123**	**(5.5)**
PENSIONS IN FORCE AT 30 JUNE	1996	1997	plus/(minus) %
Age retirement	336	445	32.4
Retrenchment (Involuntary)	591	1 737	193.9
Invalidity	330	460	39.4
Spouses & orphans	115	141	22.6
Total	**1 372**	**2 783**	**102.8**
	1995–96	1996–97	plus/(minus) %
Average Yearly Adult Pension	$15 022	$15 473	3.0
Preserved benefits in force	28 086	34 207	21.8

PSS Board

The PSS Board administers the Public Sector Superannuation (PSS) scheme in accordance with the provisions of the *Superannuation Act 1990* (the PSS Act), the Trust Deed and the Scheme Rules. It is also responsible for the management and investment of the PSS Fund.

The Board has delegated the bulk of its general administration powers and responsibilities to Commonwealth Superannuation Administration (ComSuper).

Board members

The Board consists of five Trustees—two with experience in the formulation of government policy and public administration; two nominated by the ACTU and an independent chairperson. All are appointed to the Board by the Minister for Finance under section 23 of the PSS Act.

The chairperson and the ACTU nominees are appointed for periods not exceeding three years (but are eligible for reappointment), and the other members hold office 'at the Minister's pleasure' or for such period as the Minister determines.

Members holding office at 30 June 1997 were:

Mr Ronald L. Brown (independent chairperson)—*appointed 25 July 1990, reappointed to 30 June 1998.*

Mr Brown is a consultant to both State and Federal governments and is a member of a number of government and semi-government boards and commissions. He was Secretary of DILGEA and Chief Executive of SBS. Mr Brown is also chairperson of the CSS Board.

Mr Michael J. Hutchinson—*appointed 22 June 1995; ceased 30 June 1997.*

Mr Hutchinson is the Chief Executive of the Office of Asset Sales and a member of the CSS Board. His alternate was Ms Sandra Wilson, Assistant Secretary, Commonwealth Superannuation Group, Department of Finance, Canberra. Mr Hutchinson's appointment ceased on 30 June 1997.

Mr John A. Flitcroft—*appointed 1 July 1990, reappointed to 30 June 1998.*

Mr Flitcroft is a member of the CPSU, and is Manager, Compensation Reviews (NSW) at the Department of Veterans' Affairs. He is also a member of the CSS Board. His alternate is Mr John Murphy, Public Service and Merit Protection Commission.

Ms Winsome Hall—*appointed 1 July 1996, reappointed to 30 June 1998.*

Ms Hall is a policy adviser with the Office of the Status of Women in the Department of Prime Minister and Cabinet. She is a member of the CPSU and also a member of the CSS Board. Her alternate is Mr David Irons of the Communications Workers Union, Melbourne.

Mr Peter Reynolds—*appointed 7 May 1997 to 6 May 2000.*

Mr Reynolds is a Director of a number of Local and State government bodies in NSW. He was the Chairman of the NSW State Authorities Superannuation Board and has wide experience in business and financial management through various appointments and position in the public and private sectors. He is also a member of the CSS Board.

Mr Kenneth Searson—*appointed 8 April 1992; resigned 14 February 1997.*

Mr Searson resigned in February 1997 and was replaced by Mr Peter Reynolds on 7 May 1997.

Charter 1996–97

The Board's charter is:

- to administer the Public Sector Superannuation scheme in accordance with the Act and Trust Deed; and
- to manage and invest the PSS Fund so as to maximise the real return earned on investments subject to a tolerable level of short-term volatility.

Objectives of the Board

The Board's objectives in 1996–97 were:

- to implement the Total Risk Management investment strategy to maximise the return earned on the Fund for the chosen level of risk;
- to maintain appropriate banking and related administration arrangements for the receipt of monies directed to the Fund and the payment of benefits;
- to maintain appropriate arrangements, including delegation of Board powers and functions under the Act and Trust Deed, for the proper administration of the Scheme;
- to comply with the *Superannuation Industry (Supervision) Act 1993*; and
- to develop a comprehensive strategy for communication, to PSS members, of information relating to the Fund performance and their superannuation entitlements.

Performance indicators

Indicators of performance, other than those relating to investment, are set down in the Service Level Agreement between the Board and ComSuper. Details of performance against the indicators can be found on the following pages:

- the investment performance of the Fund relative to appropriate benchmarks (see *Fund Investment*, p.14);
- the time taken to process benefit payments (see *Member Entitlements*, p.31);

- the time taken to finalise applications for Invalidity Retirement Certificates (see *Invalidity Processing*, p.36);
- the number of appeals against decisions taken under delegation and the outcome of those appeals (see *Reconsideration and Review*, p.38); and
- the success of the communications strategies used to inform members of relevant superannuation matters and of the Board's activities (see *Member Communications*, p. 43).

Secretariat to the Board

The Secretary to the Board has specific responsibilities in relation to the maintenance of the formal transcript of Board proceedings, the safe custody and control of the Common Seal, and the dissemination of Board decisions. The Secretary also acts as the conduit between the Board, the government's policy advisers (Department of Finance), the scheme administrator (ComSuper), the Board's investment adviser, PSS members, members of parliament and the media.

Secretariat services to the Board are provided by ComSuper staff. More detailed commentary can be found in the *Commissioner for Superannuation Annual Report 1996–97.*

Note of appreciation

The Board would like to acknowledge the diligence and efficiency of the staff of ComSuper and to express its appreciation for the assistance given by a range of specialists in the public and private sectors throughout the year.

Sale of CFM and TRM

In May 1996 the Federal government announced its intention to sell Commonwealth Funds Management Ltd (CFM) and its subsidiary company, Total Risk Management Pty Ltd (TRM).

TRM was established as a joint initiative between the Board and CFM to assist in the transition from CFM's monopoly position as fund manager for the PSS Fund to a deregulated environment. TRM is the principal adviser to the Board and also acts as the Board's portfolio manager.

The Board's intention had been to consider the core portfolios as the next step in the review process and, had the sale not eventuated, this review would have commenced from 1 July 1996.

In the circumstances, the Board agreed to continue with the review on a sector-by-sector basis over a 12 month period.

New owners

The Board was consulted by the Federal Office of Asset Sales during the course of the sales negotiations.

CFM was sold to Commonwealth Financial Services (CFS), the investment arm of the Commonwealth Bank of Australia. TRM was sold to the actuarial firm Towers Perrin. The separate sales of CFM and TRM were finalised in December 1996.

TRM is now a wholly-owned subsidiary of Towers Perrin. The key personnel within TRM have remained with the company which continues to provide the full range of advisory services to the Board.

Trustee company

During the 1996–97 financial year the PSS Board, in conjunction with the CSS Board, formed a company (CSS/PSS Pty Ltd) for the sole purpose of acting as a trustee for existing pooled superannuation trusts. CFM was the former trustee of these pooled superannuation trusts.

Corporate governance

The principal features of the Board's policy on corporate governance is to abide by the basic principles of corporate governance as summarised in the Australian Investment Managers' Association (AIMA) Statement of Recommended Corporate Practice. This includes setting strategic directions, reviewing business plans established by the Board and monitoring performance against those plans both directly and through its committees.

Custodial services

Following a review of custodial arrangements during the 1995–96 financial year, a new Master Custody Agreement was signed with the Chase Manhattan Bank on 2 May 1996 with a reduction in fees (the saving in fees under the new agreement for the 12 months ended 31 March 1997 was 22 per cent).

Their custodial function in relation to investment management includes settlement of trades, physical custody and safekeeping of securities, collection of dividends, and account preparation.

Chase Manhattan Bank receives all monies available for investment from ComSuper, and allocates them to the investment managers in accordance with the mandates set down by the Board.

They also hold (but do not own) the assets which comprise the Fund; collect and disburse dividends; maintain consolidated accounts and tax records for the Fund; and report to the Board on individual fund manager and aggregated investment returns.

Investment managers

All investment managers are paid a fee which is generally based on the value of assets under their control. The fee reflects the investment costs applicable to each particular sector, and the investment style (i.e. active or passive) employed by each manager.

The investment managers appointed by the Board for the 1996–97 financial year are presented overleaf.

Table 1: Investment managers at 30 June 1997	
ASSET CLASS	**INVESTMENT MANAGERS**
Australian equities	
Core	CFM AMP
Active	AMP Balanced Equity Management Pty Ltd First State Fund Managers Ltd HSBC Asset Management Australia Ltd
International equities	
Core	CFM
Asia	IDS Fund Management Ltd
USA	Brinson Partners IDS Fund Management Ltd Sasco Capital Westpeak Investment Advisors
Japan	Acadian Asset Management Inc. JP Morgan Investment Management Inc. Schroder Investment Management (Australasia) Ltd
UK/Europe	Dresdner Bank AG Mercury Asset Management Plc Schroder Investment Management (Australasia) Ltd
Emerging Markets	Blairlogie Capital Management Morgan Grenfell Funds Management Emerging Markets Management
Indexed core	Paribas Asset Management
Australian Fixed-Interest	
Core	CFM
Active	BT Funds Management Ltd Citicorp Investments Ltd
Indexed Bonds	CFM
Cash	CFM
Property	CFM
Currency overlay	Pareto Partners

Benefit design

The PSS is a defined-benefit superannuation scheme. The final benefit is calculated as a multiple of final average salary over the period prior to exit from the Scheme. Retirement benefits can be paid as lump sums with the option to exchange the lump sum (or part of it) for an indexed pension. The benefit consists of the following parts:

a) **a member-financed component**

   This part comprises the contributions paid by the member into the Fund plus accumulated interest. Interest is credited at rates determined by the Board, in line with the earnings of the Fund; and

b) **an employer-financed component**

   The employer component includes two parts–

   - The first part comprises the superannuation productivity contributions paid by the employer into the Fund plus accumulated interest.
   - The second part of the employer component is the 'benefit balance', which is determined at the time the member exits from the Scheme. The amount is the balance after the member and productivity components are deducted from the (defined) total lump-sum benefit.

Investment objective

The total benefit payable to members is set by the rules and methodology embodied in the legislated constitution of the Scheme. It does not depend on the earning rate of the Fund.

The difference between the total benefit payable to a member and the accumulated member and productivity contributions (including interest) invested in the Fund, is paid by the employer from Consolidated Revenue. The call on Consolidated Revenue will depend on the investment performance of the Fund. The better the investment performance of the Fund, the smaller the call on Consolidated Revenue. In these circumstances, it is the employer that bears the investment risk arising from the investment of the Fund.

If the call on Consolidated Revenue is to be minimised, achieving a good return over the long term is clearly of vital importance. This is explicitly recognised in the objective that the Board has set for the Fund, which is:-

> **To maximise real returns on the accumulation fund subject to a tolerable level of shorter term volatility.**

Achievement of this objective calls for attention to multiple time horizons. Fundamentally, the Fund has a long term perspective (maximising real returns on the accumulation fund), but managing shorter term volatility (variation in annual crediting rates) is also an imperative.

The investment objectives of the Fund specify the target, or acceptable levels of portfolio risk and return. They are distilled from the characteristics of the scheme (including benefit design, reserving/crediting rate policy and liability position). These are also captured in the Fund objective which is to maximise the long-term real rate of return subject to:

- a less than 20 per cent probability that nominal fund returns will be negative in any given year;
- a more than 60 per cent probability that the crediting rate will exceed CPI by three per cent in any given year; and
- a more than 70 per cent probability that the crediting rate will exceed CPI in any given year.

The above three criteria define the 'tolerable' level of volatility specified in the Fund objective.

Investment strategy

The investment strategy of the Fund is guided by a set of principles about the nature of investment management to which the Board subscribes. Those principles include:

i) attention to both the short and long term (multiple time horizons) with emphasis on the long-term behaviour of asset classes;

ii) a global view of investment opportunities;

iii) broad diversification of investments; and

iv) a portfolio structure designed to capture market returns with confidence.

Asset allocation is the most critical factor in deciding the investment strategy. It is the primary determinant of both the investment risk and investment return of the Fund. Two main decisions are involved in this process:

- asset composition—deciding the types of assets in which the Fund will invest; and
- asset weighting—deciding how much to invest in each asset type.

The investment strategy, through which the investment objectives of the Board are met, also encompasses the identification and management of all the risks associated with a portfolio of investments. These risks are:

- specific risks (those attached to individual assets);
- factor risks (those broader influences that attach to groups of related individual assets); and
- systemic risks (those attached to the whole of a particular investment market).

The Total Risk Manager's job is to identify the risks, quantify them as far as possible and manage them in combination to produce the Fund's required investment return.

The primary focus on risk (the essential component of total risk management) identifies:

- what risks exist within the investment structure;
- where those risks reside within the structure;
- how great the risks are; and
- what effect the combination of the parts has on diversifying those risks.

By applying the principles of total risk management the Board aims to achieve the following outcomes:

- to increase investment returns by taking greater risks, where those risks can be shown to be appropriately rewarded;
- to reduce risk (by diversification and other means) without decreasing return; and
- to combine investments in such a way (using options, derivatives and other means) to minimise downside risk (risk of falling prices or returns) while maximising upside return potential.

Strategic target

The Board's policy is to review the continuing effectiveness of its strategic asset allocation on an annual basis. A full tactical review is to be carried out every three years (commencing from the 1996 allocation) with the intervening years focusing on specific issues related to current market conditions. The review carried out in April 1997 focused on policy parameters, international exposure and the property portfolio.

With the assistance and advice of TRM, the Board adopted a new strategic target asset allocation in April 1996. This asset allocation was implemented during the first half of the 1996–97 financial year.

As a result of the April 1997 review, the strategic allocation to Australian shares was raised from 28 per cent to 33 per cent and the strategic allocation to property was reduced from 20 per cent to 15 per cent.

Table 2 : Strategic asset allocation and benchmark portfolio

Asset Class	Type	Asset allocation	Benchmark
Shares	Domestic	33%	ASX All Ordinaries Accumulation Index
	International	40%	MSCI World Index (ex Australia) with net dividends reinvested MSCI Emerging Markets Free Index (ex Malaysia) with gross dividends reinvested
Debt	Domestic	12%	SBC Warburg Australia Composite Bond Index & Bank Bill Index
Property	Domestic	15%	Mercer Australian Unlisted Property Index
Total Fund		100%	

Each asset class consists of core and specialist components. The core is constructed so as to provide a high probability of capturing market return whereas the specialist component allows for controlled diversity through a range of specialist active managers with different, yet complementary management styles.

Core assets are passively managed (with no active stock selection). Their purpose is to capture market returns by replicating—or tracking—the relevant sectoral index. For instance, core holdings in the Australian shares sector track the ASX All-Ordinaries Accumulation Index.

The composition and weightings of the items that make up the index changes slightly over time. The core asset managers must mirror those changes by adjusting the composition of their core portfolio. In that way, the earnings (or losses) on core assets over any period will mirror the increase (decrease) in the index over the same period.

Generally, core assets make up the bulk of a fund's investment holdings.

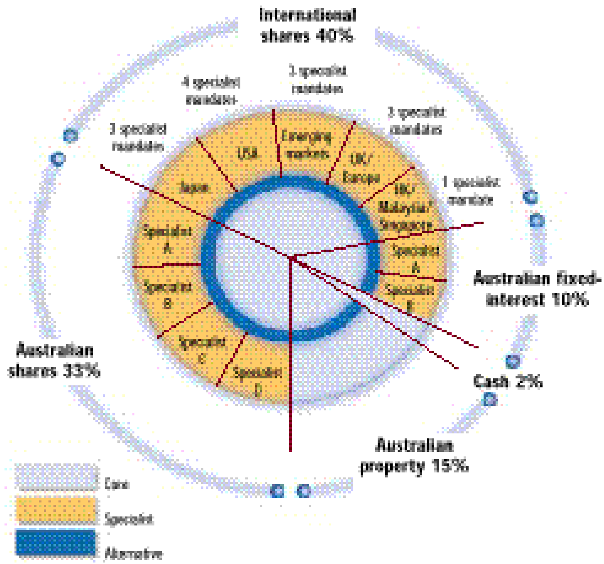
Active assets, as the name suggests, are actively managed. That is, the specialist fund managers who hold these assets must actively operate in the market, buying and selling them with a view to outperforming the sectoral index.

An exposure to emerging markets is included in the portfolio, with the level of exposure to be no more than five per cent of total portfolio assets.

The Board has also made provision for investment of up to five per cent of the total assets in non-traditional or alternative investments. These investments are to be included within sectors, with no more than ten per cent exposure in any single asset sector.

The move to increase the Fund's exposure to international equities had regard to the inherent limits on return opportunities through investment solely in the Australian equities market and the increased opportunities provided by investing in the much larger world markets. The Board's research indicates that the strategic asset weightings now adopted will position the Fund to achieve higher real rates of return for the Fund and its members over the longer term.

Chart 1: PSS Fund composition and portfolio construction at 30 June 1997



Market overview

At the end of 1996–97, the value of the Fund was $2.4 billion, an increase of $330m on last year's total. During the year, the PSS Fund recorded a return of 17.82 per cent, after tax and fees.

Equity markets performed exceptionally well around the world, culminating with share prices in Australia and all G7 countries (excepting Japan) reaching new record levels in each of the months of the June quarter, although the performance of the property sector continued to constrain results.

This strong performance in virtually all major equity markets reflects the continuation of an easy global monetary environment, a consequence of the moderate growth/low inflation conditions that prevailed in most countries and an expectation that such conditions will continue.

The key question remains whether the principles underlying the Fund's investment strategy are coming through in these one-year results. While this is a relatively brief timeframe, the trends are encouraging.

First, we have placed emphasis on equity as the asset class to carry the load in achieving the Fund's objective of maximing returns (73 per cent of the portfolio). Equity has clearly outperformed other asset classes.

Second, we have reallocated from fixed-interest to international equity, with an appropriate currency strategy. Again, the expected superiority in the performance of international equity is evident when international equity returns are combined with currency.

Third, we have continued to gradually reduce property despite consistent advice from a variety of sources that outperformance was imminent. In point of fact, property continues to underperform. Consequently, implementation of the Fund's property strategy continues to be critical.

Finally, we have set quite demanding targets for portfolio construction. The major portfolio construction position is active management. In aggregate, active management has added value although not to the level targeted at this stage.

Table 3 : PSS Fund Performance 1996–97 (after tax and fees)

Asset sector	Value of investment [1] at 30/06/96 $m	Value of investment [1] at 30/06/97 $m	Benchmark portfolio performance [2] %	Fund performance [3] %
Property	394.8	371.2	4.8	0.4
Australian equities	593.9	763.9	24.6	26.6
International equities	850.8	1 022.6	24.8	23.1
Australian Fixed-interest [4]	278.8	290.3	12.6	11.1
Total	**2 118.3**	**2 448.0**	**19.0**	**18.0**

1 The **Value of Investment** figures represent the funds under management and differ from the value of investments in the financial statements because of necessary accounting adjustments.

2 The investment performance of the **Benchmark Portfolio** represents the minimum expected performance position for the actual fund or portfolio.

3 **Fund performance** figures are after tax and management fees, and reflect income as well as realised and unrealised capital gains and losses.

4 Includes cash and indexed bonds.

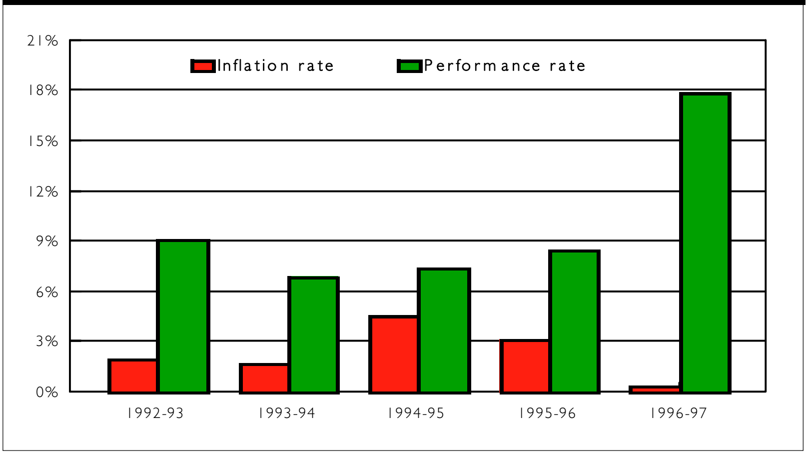
Comparison of Fund performance

When comparing the performances of superannuation funds, it is important to recognise that superannuation is, for the majority of members, a long-term investment.

Therefore, the primary objective of a superannuation fund is to maximise the expected rate of returns over the long-term while investing prudently. However, the Board must also be aware of the need to achieve acceptable levels of short-term returns (to meet the needs of exiting members), while pursuing this longer-term strategy.

A fund’s investment strategy must be consistent with the nature of its liabilities. In addition, its strategy will be affected by its risk profile, the existence (or not) of a Reserve Account, its cash flow, the scheme’s benefit design and a host of other considerations. Consequently, comparisons between the PSS Fund’s returns and the returns of other funds may be misleading without a full understanding of how all these factors influence the respective investment strategies.

Chart 2 : Fund performance compared with inflation rate 1993 to 1997



The Board believes that its objective of increasing the value of member accumulation accounts by outperforming the rate of inflation by at least three percentage points per annum over the longer term has represented a reasonable basis on which to judge the Fund's performance.

Investment information

Further information on the investment activities of the Fund can be obtained from:

The Secretary
PSS Board
PO Box 22
Belconnen ACT 2616
Phone : (02) 6252 5268 Fax : (02) 6252 7965

Note on calculations

The Fund earning rates quoted in this report differ from the rates calculated by ComSuper for annual crediting rate purposes. Time-weighted rates of return are used within the investment management industry as the basis of comparing the performance of different funds in which cash flows can vary considerably. The investment manager usually cannot control the timing or the amount of contributions to the Fund. Because the time-weighted rate eliminates the impact of money flows into or out of the fund, it is an effective means of appraising the fund manager's ability to make the Fund's assets perform.

The returns calculated for crediting rate purposes are money-weighted i.e. the return is calculated by reference to the amount and the timing of cash flow during a given time period. This approach gives an effective measure of the Fund's rate of growth, giving full weight to the impact of cash flows on Fund assets.

Annual crediting rates also differ from earning rates because of the working of the Reserve Account (p. 29) and the Deferred Losses Account (p. 30).

Crediting rate policy

The key features of the crediting rate policy are:

- the target rate is the June-to-June CPI plus three per cent;
- the Reserve Account bounds are plus/minus five per cent of Fund assets (based on the size of the Fund at the end of the financial year); and
- there are proportional adjustments into and out of the Reserve Account.

At the end of the year, the earning rate for the year is determined and compared to the target rate as follows:

– if the earning rate is *higher* than the target rate, the crediting rate will be reduced in proportion to the reserve but subject to a limit on the amount which can be transferred to the Reserve.

– if the earning rate is *lower* than the target rate, the crediting rate will be increased to the target rate by transferring funds from the Reserve Account.

Transfers to and from the Reserve Account are subject to the restriction that the balance of the Reserve Account cannot exceed five per cent of the balance of the Fund, nor can it be less than minus five per cent of the Fund, at the end of the financial year.

If the Reserve Account is *greater than* five per cent of the balance of the Fund at the end of the financial year, the excess above five per cent is used to raise the crediting rate.

The lower limit on the Reserve Account does not apply if a larger transfer is needed to ensure that the crediting rate is not negative.

Crediting rates

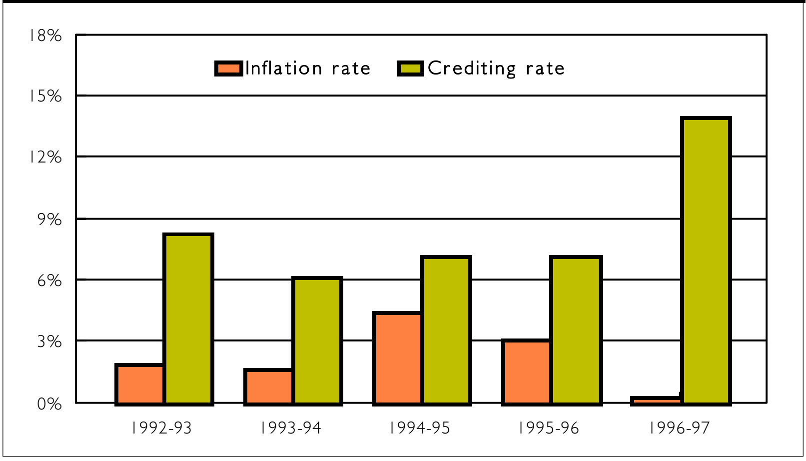
Every year, interest is credited to members' accumulated contributions at rates determined by the Board. Table 4 lists the annual crediting rates for the past five years.

Table 4 : Annual crediting rates 1993 to 1997

Financial year	Crediting rate %
1992–93	8.3
1993–94	6.2
1994–95	7.2
1995–96	7.2
1996–97	14.0

Over the years, the annual crediting rate has generally outperformed the rate of inflation, as the following chart shows.

Chart 3 : Crediting rates compared with inflation rates 1993 to 1997



Reserve Account

The Board is precluded by legislation from declaring a negative crediting rate. Given this prohibition, the options available to the Board to reduce the volatility of returns and guard against negative returns include:

- investment in conservative products such as cash-based products or capital-stable products with high cash content; or
- investment in capital-protected products (such as capital-guaranteed funds offered by life offices).

In both cases, the expected long-term return is reduced as a trade-off for less volatile returns.

Consequently, the Board has adopted a more growth-oriented, higher expected return investment strategy coupled with a reserve account to smooth out fluctuations in annual crediting rates. Under this approach, the rates credited to members' accounts may differ from the actual rates earned on the Fund's investments. In years when high returns are earned, part of the investment earnings are transferred to the Reserve Account, at the expense of a reduction in the rate credited to members. In years when poor or negative returns are earned, transfers from the Reserve are used to 'top up' the interest rate credited to members.

The advantage of smoothing lies in the limitation of downside risk for those nearing retirement, which allows a higher investment risk profile than might otherwise be the case. A higher risk profile should deliver higher real returns to all members over the long term.

This year, a net $114.6m was transferred to the Reserve. The balance of the Reserve Account at 30 June 1997 was $142.8m.

Deferred Losses Account

The annual crediting method also entails small quarterly transfers from earnings to the Deferred Losses Account (DLA) to continue the process of reducing the balance of that account to zero by 1 July 1999. The DLA was created on 1 July 1984 as a means of spreading over 15 years the effect of a one-off loss in Fund assets arising from a change to market-value accounting for determining the value of the Fund's assets.

This year, a net $1.1m was transferred to the DLA. The balance of the DLA at 30 June 1997 was $5.8m.

Exit rates

When a member leaves the Scheme, an exit rate of interest is applied to cover the period between the date of the last annual crediting rate and the member's date of exit. Exit rates are determined by the Board quarterly, in a manner consistent with the method for determining annual crediting rates. The exit rates for 1996–97 are shown in Table 5 below.

Table 5 : Exit rates declared in 1996–97

Effective Date	Exit rate (annualised)
9 September 96	6.2%
11 December 96	6.3%
17 February 97	7.4%
12 May 97	7.0%

Each new exit rate replaces the previous one. For example, members who exited on or after 12 May 1997 had an interest rate of 7.0 per cent per annum applied to their accumulated contributions for the period from 1 July 1996 until their date of exit.

General introduction

The Board has delegated the bulk of its general administrative powers and functions to the Commissioner for Superannuation and to staff of ComSuper.

As the Board's scheme administrator, ComSuper's major areas of activity encompass the calculation and payment of benefits (including the significant area of invalidity benefits), the maintenance of records of contributors and pensioners, the receipt of and accounting for contributions from employing agencies in respect of their employees, the reconsideration and review of decisions on entitlements and the provision of information to the membership.

The Trustees set the standards of performance for ComSuper in its delivery of services to members for these areas of activity, and the Trustees also monitor the administrator's performance.

A detailed description of all ComSuper activities is contained in the *Commissioner for Superannuation Annual Report 1996–97.*

Members' contributions

Members may choose to contribute between two and 10 per cent of their salary. They may vary their contribution rate at any time, which enables them to adjust to changing financial circumstances.

In 1996–97, ComSuper received contributions totalling $341.4m, which comprised $229.0m in member contributions and $112.4m in productivity contributions. Benefits paid from the Fund during the year totalled $344.9m and transfers from other schemes totalled $434.8m, giving a net contributions flow into the Fund for 1996–97 of $431.3m.

Number of members

At 30 June 1997, the PSS had 114 123 members—a decrease of 5.5 per cent over the population at 30 June 1996.

Table 6 : Scheme membership 1993 to 1997

Year ending	Male	Female	Total
30 June 1993	43 219	55 491	98 710
30 June 1994	45 441	58 700	104 141
30 June 1995	47 008	60 426	107 434
30 June 1996	53 574	67 200	120 774
30 June 1997	50 271	63 852	114 123

Note: *As a result of the Choice campaign conducted between 1 March 1996 and 2 September 1996, members who elected to transfer from the CSS to the PSS became members of the PSS effective from 1 March 1996. If a member so elected but did so after 30 June 1996, that member would reflect as being both a member of the CSS and the PSS on 1 July 1996. This is due to the date of cessation in the CSS being later than 30 June 1996 but the date of commencement in the PSS being prior to 1 July 1996. Thus, the figures for year ending 30 June 1996 and 30 June 1997 do not properly account for scheme transfers made after 1 July 1996 which are effective from 1 March 1996.*

Entry medical requirements

New PSS members must complete a comprehensive medical questionnaire—a *Confidential Medical and Personal Statement*, or CMAPS—and send it direct to ComSuper within 14 days of commencing membership. In the case of temporary or casual employees electing to join the Scheme, the form must be sent to ComSuper within 14 days of electing to join the PSS.

The completed form is examined by a delegate of the Board who, on the basis of information provided by the member, generally determines the member’s benefit status. If the delegate considers the member to be healthy enough to perform his/her duties for three years without taking excessive sick leave, the member will be classified as a full benefits member.

However, if the responses on the CMAPS indicate the existence of one or more conditions that suggest that the member may not be fit for three years' employment (without taking excessive sick leave), the delegate may classify the new entrant as a *Limited Benefits Member*. In a small number of cases, the delegate requires additional medical information to determine the member's PSS medical status. New entrants may be required to attend a medical examination. Where the member has already had a medical examination for employment purposes, ComSuper may seek the member's authority to have access to that report to avoid the need for a further medical examination.

If a limited benefits member dies, or is retired or redeployed for any medical reason within three years of becoming a member, the member's benefit is limited to a lump-sum refund of his/her accrued benefit. Limited benefits status ceases to have effect after three years' membership.

During the year, 8866 CMAPS were processed with only 119 (1.3 per cent) being accorded limited benefit status. The number of new entrants with a limited benefits classification compared with the previous year has increased by about 80 per cent.

Additional death and invalidity cover

From 1 July 1990, eligible members have been able to take out additional death and invalidity cover under a group life policy effected between ComSuper and a life office. Since 1 July 1993, this cover has been provided by National Mutual.

At 30 June 1997, there were 1375 members paying premiums for additional death and invalidity cover, compared with 1011 at 30 June 1996. Of those, 1335 were covered at standard rates and 40 were covered with a loading. (A loading is where the life office requires the member to pay a premium above the standard life cover.)

The gross amount of cover has seen a similar increase, growing from \$69.8 m to \$95.6 m. The average value of additional cover was \$69 508 per member. The average age of persons accepted for additional death and invalidity cover was 43 years.

Pensions in force

There were 2783 pensions in force at 30 June 1997, an increase of 102.8 per cent from the 1372 pensions in force at 30 June 1996. At 30 June 1997, the annual PSS pension liability was $43.06 million. Table 7 below gives a breakdown of those pensions by type and their annual liability.

Table 7 : Pensions in force at 30 June 1997

Type of pension	Number	Annual Liability
Age	445	$ 5.89m
Involuntary retirement	1 737	$27.16m
Invalidity	460	$ 7.80m
Spouses & orphans	141	$ 2.21m
Total	**2 783**	**$43.06m**

Benefit applications

The year 1996–97 saw a significant increase in the number of benefit applications received in ComSuper, primarily as a result of significant retrenchment programs initiated by public sector agencies. ComSuper received more than 9200 benefit applications in the first six months of the financial year or more than 1500 per month.

Benefit processing

The high rate of benefit applications had a serious effect on benefit application turnaround times. ComSuper, in its service level agreement with the Trustees, agrees to process 60 per cent of PSS member benefits within 10 days of the later of the date of exit or the date all documentation necessary for processing is received. Although ComSuper diverted experienced processing staff from other areas of the office and implemented a significant overtime program, it was unable to maintain the agreed turnaround times for the period from August 1996 to March 1997 given the significant increase in workload, with the number processed within the agreed standard falling to as low as 18 per cent in October 1996.

In the early part of 1997, the number of benefit applications declined such that from April onwards, ComSuper was able to achieve the benefit turnaround time standards once again.

Exits by type

During 1996–97, 14 774 members left the scheme. More than 56 per cent of the exits came from the retrenchment category. Table 8 gives a summary of the contributor exits.

Table 8 : Exits by type 1996–97

Type	Number
Age retirement	554
Retrenchment (involuntary)	8 322
Invalidity	149
Death	55
Resignation and other	5 694
Total	**14 774**

Payment of invalidity benefits

Members who are totally and permanently incapacitated, to the extent that they are unlikely to work again in a position for which they are reasonably qualified by education, training or experience (or could become so after retraining), may be retired on invalidity grounds and become entitled to payment of invalidity benefits. The invalidity retirement process is designed to ensure a thorough assessment of a person's condition and to fully consider prospects of rehabilitation and/or retraining before the Board issues an invalidity retirement certificate. The success of this assessment process is borne out by the fact that the Board, or a delegate, approved invalidity retirement for more than 90 per cent of applications considered.

The legislation provides for pre-assessment payments to be made, to ensure that a person who is (or is likely to become) totally and permanently incapacitated is not left without income while his or her case is assessed.

Pre-assessment payments

Applications for pre-assessment payments and/or the issue of an invalidity retirement certificate are normally made to ComSuper through the applicant's employer. If the applicant wishes to be paid pre-assessment payments, the employer must include a medical report completed by a Health Services Australia medical advisor (or other Board-approved medical practitioner) who has examined the person and considers that the person is, or is likely to become, totally and permanently incapacitated.

During 1996–97, pre-assessment payments were approved in respect of 137 applicants and one applicant was refused pre-assessment payments on the ground that there was little likelihood that he/she would be unable to work again.

Assessment panel

The decision-making process requires the Board to engage an assessment panel, experienced in assessing invalidity claims for superannuation purposes, to help the Board determine whether a person is totally and permanently incapacitated. During 1996–97, assessment panel services were provided by Disability Claims Management & Counselling Service (DCMC). Of the 178 cases considered by DCMC, 150 were approved and 18 were refused. Ten cases were deferred for further consideration.

Board decisions

When all the necessary information is available, ComSuper is in a position to place the matter before the Board (or in certain circumstances to approve the invalidity retirement under delegation from the Board). At this time, the Board is required to decide whether to approve the retirement and, if so, to issue a certificate having regard to:

(a) the advice of the assessment panel; and

(b) the ‘practicality’ of the person being able to find a job for which he or she is qualified or could become qualified after retraining.

In 1996–97, 149 invalidity retirement certificates were approved. Of those, 12 were fast-tracked by the invalidity assessment panel in less than one week.

The Board is satisfied that ComSuper is meeting the standards set for turnaround times in the processing of invalidity benefits.

Role of the Board

Decisions of the Board and its delegates are subject to internal reconsideration and external review. These processes are managed by ComSuper.

Internal reconsideration

A person affected by a decision of the Board or a delegate may apply in writing to have it reconsidered. If the Board took the decision, the application must be supported by evidence not previously known to the Board. A fee of $150 is payable. If the appeal is successful or withdrawn, the fee is refunded.

Decisions are reconsidered on the basis of new evidence provided by the applicant or obtained by ComSuper. A request for reconsideration of a decision is usually referred to the relevant Reconsideration Advisory Committee (RAC)[1] for examination. The RAC's recommendation is taken into account by the Board in deciding whether to affirm or vary the original decision. The Board can also refer a decision to the RAC on its own motion. Each applicant receives a comprehensive written statement of reasons for the Board's decision on reconsideration.

Requests for reconsideration are treated as complaints for purposes of Section 101 of the SIS Act.

1 Two RACs have been established. One reviews delegates' decisions and normally consists of any two of the Commissioner for Superannuation, her deputy and another SES officer. The other reviews decisions of the Board and consists of two Trustees.

Thirty two applications for reconsideration were received, compared with 24 last year. Six applications concerned the limited benefits status of members; four concerned benefits payable to spouses or children; four concerned the early release of preserved benefits. The others included applications concerning invalidity retirement and mode of exit from the Scheme.

Legislative changes

To streamline the resource intensive reconsideration process, the following legislative changes are being sought at the request of the PSS and CSS Boards:

- removal of provisions prohibiting the Boards from delegating their power to reconsider decisions;
- retention of the RACs as presently constituted, but as decision-making bodies with powers to reconsider decisions identical with those currently possessed by the Boards;
- removal of the requirement that an RAC make a recommendation to a reconsideration decision-maker;
- provision of power to dismiss an application for reconsideration or treat an application as having been withdrawn where the Board considers it trivial, misconceived or without substance; and
- provision of a time limit, of 28 days or such further period as the Board allows, in which to request reconsideration.

Table 9 : Reconsideration applications received and outcomes 1996–97	1995–96		1996–97	
	Delegate's decisions	Board's decisions	Delegate's decisions	Board's decisions
Brought forward	22	2	29	3
Received	26	4	23	7
Withdrawn or lapsed	4	0	11	2
Decisions affirmed	4	2	11	1
Decisions varied	3	0	3	0
Decisions set aside	8	1	5	1
Resolved	19	3	30	4
Carried forward [1]	29	3	22	6

1 The cases carried forward were under investigation by ComSuper or with the RAC.

External review

Superannuation Complaints Tribunal

Following the PSS Board's election on 29 June 1995, the PSS became a regulated superannuation fund for SIS purposes.

Decisions taken by the PSS Board are reviewable by the Superannuation Complaints Tribunal (SCT), which was established under the *Superannuation (Resolution of Complaints) Act 1993* (the SRC Act).

When it commenced operation on 1 July 1994, the SCT was precluded by regulations from dealing with complaints that involved the assessment or evaluation of medical evidence and/or consideration of a person's incapacity. This restriction was subsequently removed by regulations and the *Superannuation Industry (Supervision) Legislation Amendment Act 1995* (the SISLA Act), which took effect on 12 December 1995, amended the SRC Act to enable the SCT to review medical complaints.

However, under the SRC Act as amended by the SISLA Act, the SCT cannot deal with the PSS Board decisions relating to the payment of a disability benefit because of total and permanent incapacity if :

- the primary decision was made prior to 1 November 1994;
- the primary decision was made on or after 1 November 1994 and the complaint was not lodged with the SCT within one year from the time the primary decision was made; and
- before the date of the primary decision, the person permanently ceased working because of a physical or mental disability that gave rise to the claim for disability benefit, and the person did not lodge the claim with the Board within one year after he/she permanently ceased employment.

Under the SRC Act, a party to a proceeding before the SCT may appeal to the Federal Court on a question of law from any decision of the SCT in that proceeding.

Complaints lodged with the SCT

During the year, seven complaints were lodged with the SCT against the PSS Board and three were carried over from the previous year. Of the four complaints resolved during the year, the SCT affirmed one decision and treated the other three applications as withdrawn on the basis that they were misconceived. Three of the complaints involved the early release of the employer component of the members' preserved benefit, and one involved the recovery of shortpaid contributions. Six matters were on hand as at 30 June 1997.

Federal Court

Decisions taken in the administration of the PSS are subject to review by the Federal Court under the *Administrative Decisions (Judicial Review) Act 1977* (the AD(JR) Act). Appeals to the Federal Court may be based on any of the legal grounds set out in sections 5, 6 and 7 of the AD(JR) Act, including:

- errors of law;
- improper exercise of power;
- denial of the rules of natural justice;
- failure to observe procedures; or
- unreasonable delay in making a decision.

The ambit of decisions which may be reviewed under the AD(JR) Act includes decisions made by the PSS Board and its delegates. Four appeals were lodged by two applicants with the Federal Court during 1996–97 involving the early release of the employer component of the member’s preserved benefit. One applicant lodged an appeal with the Federal Court after being unsuccessful at the SCT. The appeal was dismissed by a single judge of the Federal Court. The applicant lodged a further appeal with the Full Federal Court which affirmed the judgement of the single judge. The applicant subsequently lodged an application for leave to institute proceedings under the AD(JR) Act out of time. This case remains outstanding as at 30 June 1997.

SIS requirements

As a regulated fund under the SIS Act, the Fund must comply with all the standards as set out in the SIS regulations. One of the major requirements is to maintain ongoing communication with scheme members, giving assurance that the superannuation industry operates in a fair, honest and open manner.

The Board believes that it is important to keep members informed of developments in superannuation that might affect their future entitlements.

As part of its ongoing communication campaign, each year the Board distributes an *Annual Report to Members*, providing details of Fund performance and information about developments that have occurred during the year. This report is prepared with assistance from ComSuper.

Information statements

Along with the Board's report, members (including those members who have a preserved benefit in the Fund) are sent an *Annual Information Statement* which shows their share in the Fund, including the amount of contributions they have paid, the amount of productivity contributions paid by their employer and the interest added to both components.

Scheme publications

ComSuper, on the Board's behalf, also provides members with publications that help them to find out more about their superannuation scheme. These publications include a comprehensive information book, *The Super Book*, and a series of leaflets explaining specific aspects of the Scheme. The leaflets are regularly updated to reflect changes that occur from time to time.

New PSS members are issued with a superannuation information kit called *The Super Kit*. The kit contains selected leaflets that may be of interest to the member plus a comprehensive list of additional information available from their personnel section. The kits are issued to new members by their employer.

As well, ComSuper keeps agency personnel sections informed of administrative changes through a monthly newsletter, *ComSuper News*.

The cost of producing and distributing these publications is charged to ComSuper's budget appropriation.

ComSuper has developed a comprehensive home page on the Internet and is increasingly using this new technology as a means of improving communications with scheme members.

Comsuper's website address is **http://www.comsuper.gov.au**

Inquiries about any of the publications mentioned above or our Website can be addressed to:

Schemes Promotion Group
ComSuper
PO Box 22
Belconnen ACT 2616
Phone : (02) 6252 7685 Fax : (02) 6252 7838

Key function

The combined PSS/CSS Audit Committee advises both Boards of Trustees on accountability and audit-related matters.

Responsibilities and role

The Committee's responsibility is to assure the Boards that their financial statements are based on appropriate accounting concepts, systems and techniques; that the audit arrangements within service-providing agencies (ComSuper, fund managers, master custodian and the Department of Finance) are operating effectively, and that appropriate fraud control strategies are in place.

The Audit Committee is appointed by the Boards and comprises three members, at least two of whom are members of both the PSS and CSS Boards.

The term of appointment of individual members of the Audit Committee is at the discretion of the Boards.

Terms of reference

The terms of reference of the Audit Committee are as follows:

- The Audit Committee is the point of communication between the Boards and the Internal Audit Committees of ComSuper and with the Australian National Audit Office (ANAO).
- The Committee meets when its members think it is necessary (but, in any event, not less than twice per year). In 1996–97, the Audit Committee comprising Mr Angus McKenzie (chair), Ms Winsome Hall and Mr Michael Hutchinson met on four occasions.

- The Audit Committee reviews:
  - financial statements with both internal and external auditors prior to their approval by the Boards;
  - accounting policies adopted or any changes which are made or contemplated by ComSuper, and which affect the Boards' areas of responsibility;
  - the annual audit plans of ComSuper where they relate to areas of Board responsibility;
  - the audit reports of major audits undertaken;
  - the extent to which internal audit recommendations are implemented; and
  - interim financial information.
- The Committee provides a regular report to the Boards as to whether the internal controls employed by ComSuper and other service providers give reasonable assurance that the Boards' objectives and goals are being met efficiently and economically.
- With the agreement of the Boards, the Committee may initiate specific audit investigations.

The Audit Committee participated in the development of ComSuper's forward internal audit program for 1997–98 and monitored the progress of audits undertaken in the course of the 1996–97 program.

Computer systems upgrade

A major objective of the Board's Audit Committee was to monitor the financial statement preparation and audit process progressively during the year. The Committee needed to assure itself that all reasonable efforts were made by the administrator to minimise the risk of qualification pending the completion of its computer systems redevelopment project.

More detail in relation to this matter can be found in the Financial statements on page 63.

Preservation arrangements

The Government has made a number of important announcements aimed at substantially increasing preservation requirements. These measures will significantly reduce access to lump sum benefits before retirement. Existing rights to take benefits in the form of pension, however, are not affected. The main changes will be:

(a) The preservation age will be gradually increased from 55 so that by 2025 it will be 60 years for anyone born after 30 June 1964. The phase in schedule will be:

People born	Preservation age
Before 1 July 1960	55
1 July 1960 - 30 June 1961	56
1 July 1961 - 30 June 1962	57
1 July 1962 - 30 June 1963	58
1 July 1963 - 30 June 1964	59
After 30 June 1964	60

(b) From 1 July 1999, all future member contributions and interest earnings will be preserved. It is expected that transitional arrangements will apply such that existing members will retain access to their accumulated member component as at 30 June 1999. The productivity benefit is already required to be preserved.

(c) Until 30 June 1999 the Federal Government will allow access to superannuation redundancy benefits for Commonwealth employees who are made redundant as a consequence of their jobs being outsourced or the sale of the enterprise for which they work. From 1 July 1999, however, the employer-financed component of <u>all</u> redundancy benefits will have to be preserved. This restriction will apply irrespective of the reason for the redundancy.

Choice of Fund

- From 1 July 1998 all new Commonwealth employees will have their employer superannuation paid into their chosen complying superannuation fund or Retirement Savings Account (RSA) instead of the Public Sector Superannuation (PSS) scheme. The PSS will be closed to new members from that date.
- From 1 July 2000, members of the PSS will have the choice of remaining in their scheme, with no change to existing arrangements or, to cease membership and have future employer superannuation paid to a complying superannuation fund or RSA of their choice.
- There will be no change to superannuation funding provided to agencies but employer contributions for new employees and employees who leave the PSS will be able to be negotiated with the employer subject to a safety net (minimum) of the Superannuation Guarantee Rate.

The interaction between the new arrangements and workplace agreement making will be considered as part of the implementation details to be developed and announced at a later date.

Taxation rebate

Also as part of the budget the government announced that a taxation rebate will be available in respect of undeducted member superannuation contributions and net personal income from other savings and investments up to an annual cap of $3000. In 1998-99 a transitional rebate of 7.5 per cent will apply providing an initial rebate of up to $225. From 1 July 1999, the rebate rate will increase to 15 per cent providing a maximum rebate of $450 per annum.

Collection of Tax File Numbers

An amendment to the *Superannuation Industry (Supervision) Act 1993* (SIS), effective from 17 February 1997, required the Board to ask new members for their tax file numbers (TFNs). The Australian Taxation Office has facilitated the collection of TFNs for new members by including a question on the employment declaration form which allows new employees, when completing this form, to agree to their TFN being passed on to the administrators of their superannuation fund. When the TFN is entered into the member's pay system, and if the member agrees, the TFN is electronically transmitted to ComSuper.

SIS also requires that superannuation funds ask their existing members to provide their TFN. Requests for TFNs from existing members are required to be made within seven days of the 1996–97 Information Statement being issued to members. It is proposed to seek TFNs from existing members through a one-off exercise in September/October 1997. Members will be required to agree to their TFN being transmitted from their pay system to ComSuper.

The Board will use members' TFNs for superannuation purposes which will enable tax on eligible termination payments to be at concessional rates;

- multiple superannuation accounts to be amalgamated;
- the TFN to be passed onto the ATO to assist in locating any unclaimed moneys;
- the TFN to be passed onto another superannuation fund receiving the member's rollover; and
- the TFN to be passed onto the ATO with details of the member's surchargeable contributions for assessment of any surcharge liability.

Superannuation Surcharge

A package of legislation implementing the superannuation surcharge came into effect on 5 June 1997. The surcharge legislation imposes a surcharge of up to 15 percent of member's surchargeable contributions where the member's adjusted taxable income exceeds $70 000.

Surchargeable Contributions

Surchargeable contributions in respect of the PSS are defined as salary for superannuation purposes multiplied by a Notional Surchargeable Contribution Factor (NSCF). The NSCF is determined by the Australian Government Actuary. Surchargeable contributions are intended to represent the cost of employer financed benefits accruing to the member.

ComSuper, as the Board's administrator, will advise the ATO of the amount of each member's surchargeable contributions for the period 21 August 1996 to 30 June 1997. This information is due to be provided to the ATO by 15 December 1997. Surchargeable contributions for each subsequent financial year are to be provided to the ATO by 30 October of that year.

Tax File Number for Surcharge Purposes

Identification of members for the purposes of the surcharge will be by means of the tax file number (TFN) which will be forwarded to the ATO along with the amount of surchargeable contributions. The ATO will cross match the information supplied with tax returns lodged by tax payers. This will enable the ATO to determine the member's adjusted taxable income and assess liability for the surcharge.

Adjusted Taxable Income

The ATO will determine the member's adjusted taxable income by adding the surchargeable contributions to the member's taxable income. If adjusted taxable income is greater than $70 000 the ATO will determine an amount of surcharge payable in respect of that member.

Paying the Surcharge

ComSuper, as the Board's administrator, will maintain a surcharge account for each member. Where the surcharge account is in debit at 30 June each year, interest at the 10-year bond rate will be applied to that debit amount.

If the surcharge account is in debit at the time a benefit becomes payable the debit amount will be deducted from the member's benefit and paid to the ATO. Alternatively members can make periodic payments to ComSuper to reduce the amount of their surcharge debit.

Appendixes

Appendix A
Legislation matters

Determinations

Four determinations were made by the PSS Board during the year which set various interest rates during scheme membership.

One further determination was made which set the rate of interest applicable to late-remitted employer contributions.

11th PSS Amending Deed

There were various changes made by the 11th amending deed, which came into effect from 18 December 1996, concerning the following matters:

- appointment of independent trustee;
- sales or transfers of non-Commonwealth agencies;
- salary of ex-casual workers;
- retrospective contribution rates;
- benefit options;
- death benefit options;
- preserved benefits;
- partial invalidity pension;
- transfer benefits;
- unclaimed benefits; and
- maximum benefits.

Appendix B
Departments and approved **authorities**

At 30 June 1997, the following departments and authorities were employers of people who were eligible to contribute to the PSS.

Departments

Administrative Services
Attorney-General's
Communications and the Arts
Defence
Employment, Education, Training and Youth Affairs
Environment, Sport and Territories
Finance
Foreign Affairs and Trade
Health and Family Services
Immigration and Multicultural Affairs
Industrial Relations
Industry, Science and Tourism
Parliamentary:
- House of Representatives
- Joint House
- Parliamentary Library
- Parliamentary Reporting Staff
- Senate

Primary Industries and Energy
Prime Minister and Cabinet
Social Security
Transport
Treasury
Veterans' Affairs

Approved authorities

Aboriginal and Torres Strait Islander Commercial Development Corporation*
ACTEW Corporation Ltd*
ACT Institute of Technical and Further Education
Albury Wodonga Development Corporation
Anglo-Australian Telescope Board
Australia Council
Australian Broadcasting Corporation
Australian Capital Territory
Australian Dairy Corporation
Australian Dried Fruits Corporation
Australian Film Commission
Australian Film, Television and Radio School
Australian Fisheries Management Authority*
Australian Foundation for Culture and the Humanities Ltd*
Australian Honey Board
Australian Institute of Criminology
Australian Institute of Marine Science
Australian International Hotel School*
Australian Marine Science and Technology Limited*
Australian Maritime Safety Authority*
Australian National Gallery
Australian National Railways Commission
Australian National Training Authority*
Australian Nuclear Science and Technology Organisation
Australian Pork Corporation
Australian Sports Commission
Australian Sports Drug Agency*
Australian Securities Commission
Australian Tobacco Marketing Advisory Committee
Australian Tourist Commission
Australian Trade Commission
Australian Trade Union Training Authority
Australian Wheat Board
Australian Wine and Brandy Corporation
Calvary Hospital ACT Incorporated
Canberra Institute of the Arts
Centralian College
Civil Aviation Safety Authority*
Commonwealth Funds Management Limited*
Commonwealth Scientific and Industrial Research Organisation
Construction Industry Development Agency
Cotton Research and Development Corporation*
Dairy Research and Development Corporation*
Energy Research and Development Corporation*

Export Finance and Insurance Corporation*
Fisheries Research and Development Corporation*
Forest and Wood Products Research and Development Corporation*
Grains Research and Development Corporation*
Health Insurance Commission
High Court of Australia
Horticultural Research and Development Corporation
Housing Loans Insurance Corporation
Indigenous Land Corporation*
Institute of Family Studies
Land and Water Resources Research and Development Corporation*
Law Courts Limited
Law Reform Commission
Legal Aid Commission (ACT)
Meat Research Corporation (formerly the Australian Meat and Livestock Research and Development Corporation)
Murray Darling Basin Commission
National Registration Authority of Agriculture and Veterinary Chemicals*
National Standards Commission
National Training Board
Parliament House Construction Authority
Pig Research and Development Corporation*
Pipeline Authority
Private Health Insurance Administration Council*
Private Health Insurance Complaints Commissioner*
Rural Industries Research and Development Corporation
Snowy Mountains Hydro-Electric Authority
Special Broadcasting Service*
Sydney Symphony Orchestra Holdings Pty Limited
Sugar Research and Development Corporation
Totalcare Industries Limited*

* These bodies have been declared Approved Authorities under the *Superannuation Act 1990*. All other bodies became Approved Authorities under the *Superannuation Act 1990* by virtue of being Approved Authorities under the *Superannuation Act 1976* on 30 June 1990. Amended to Superannuation (PSS) Approved Authority Inclusion Declaration (Amendment) Declaration, Statutory Rules 1997 No. 174 of 30 June 1997.

Appendix C
Eligible superannuation **schemes**

A Transfer Value may be paid to a superannuation scheme which has been declared by the Minister for Finance and the Board to be an eligible superannuation scheme for the purposes of the Public Sector Superannuation (PSS) scheme (Rule 8.2.5).

The following schemes have been declared eligible.

- Superannuation schemes established under the following acts:
  Superannuation (State Public Sector) Act 1990 (QLD);
  Parliamentary Contributory Superannuation Act 1948; and
  Defence Force Retirement and Death Benefits Act 1973.

- The superannuation schemes known as:

  Army and Air Force Canteen Service Superannuation Scheme;
  Australian Wool Corporation Provident Fund;
  AUSSAT Superannuation Fund;
  AV Super (previously known as the CAA Staff Superannuation Fund);
  Gladstone Area Water Board Staff Superannuation Scheme;
  Gladstone Port Authority Staff Superannuation Scheme;
  Gold Coast Waterways Staff Superannuation Scheme;
  Government Officers' Superannuation Scheme (GO Super) (Queensland);
  Livestock and Meat Authority of Queensland Superannuation Scheme;
  Northern Territory Government and Public Authorities Superannuation Scheme;
  Queensland Ambulance Transport Brigade Staff Superannuation Scheme;
  Queensland Electricity Supply Industry Superannuation Scheme;
  Queensland Industry Development Corporation Superannuation Scheme;
  Queensland Local Government Employees Superannuation Scheme;
  Queensland Parliamentary Contributory Superannuation Scheme;
  Queensland Police Superannuation Scheme;
  Queensland State Service Superannuation Scheme;
  Suncorp Insurance and Finance Superannuation Plan;
  Superannuation Scheme for Australian Universities (SSAU);
  Townsville Port Authority Staff Superannuation Scheme; and
  University of Newcastle Staff Superannuation Scheme.

Appendix D
List of **abbreviations**

AAS	Australian Accounting Standard
ACTU	Australian Council of Trade Unions
AD(JR) Act	*Administrative Decisions (Judicial Review) Act 1977*
ANAO	Australian National Audit Office
ASX	Australian Stock Exchange
ATO	Australian Taxation Office
CFM	Commonwealth Funds Management Ltd
ComSAS	Commonwealth Superannuation Administration System
ComSuper	Commonwealth Superannuation Administration
CPI	Consumer Price Index
CPSU	Community and Public Section Union
CSS	Commonwealth Superannuation Scheme
CSS Act	*Superannuation Act 1976*
DCMC	Disability Claims Management & Counselling Service
DILGEA	Department of Immigration, Local Government and Ethnic Affairs
DLA	Deferred Losses Account
GBE	Government Business Enterprise
ISC	Insurance and Superannuation Commission
MSCI	Morgan Stanley Capital International
PSMPC	Public Service and Merit Protection Commission
PSS	Public Sector Superannuation (scheme)
PSS Act	*Superannuation Act 1990*
RAC	Reconsideration Advisory Committee
RBL	Reasonable Benefit Limit
SBS	Special Broadcasting Service
SIS Act	*Superannuation Industry (Supervision) Act 1993*
SCT	Superannuation Complaints Tribunal
SRC Act	*Superannuation (Resolution of Complaints) Act 1993*
TRM	Total Risk Management Pty Ltd

Appendix E
Financial **statements**

Australian
National
Audit
OFFICE

INDEPENDENT AUDIT REPORT
COMMONWEALTH SUPERANNUATION BOARD OF TRUSTEES NO. 1

To the Minister for Finance

(A) Financial Statements

Scope

I have audited the financial statements of the Public Sector Superannuation Scheme (PSS) which includes the Commonwealth Superannuation Fund No. 1 (PSS Fund), for the year ended 30 June 1997. The financial statements comprise:

- Statement of Changes in Net Assets
- Statement of Net Assets
- Notes to and forming part of the Financial Statements, and
- Statement by the Trustees.

The Commonwealth Superannuation Board of Trustees No. 1 is responsible for the preparation and presentation of the financial statements and the information they contain. I have conducted an independent audit of the financial statements in order to express an opinion on them to you, the Minister for Finance.

The audit has been conducted in accordance with Australian National Audit Office Auditing Standards, which incorporate the Australian Auditing Standards, to provide reasonable assurance as to whether the financial statements are free of material misstatement. Audit procedures included examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial statements, and the evaluation of accounting policies and significant accounting estimates.. These procedures have been undertaken to form an opinion as to whether, in all material respects, the financial statements are presented fairly in accordance with Australian Accounting Standards, other mandatory professional reporting requirements (Urgent Issues Group Consensus Views) and statutory requirements so as to present a view of the Fund and the Scheme which is consistent with my understanding of its net assets and changes in net assets.

The audit opinion expressed in this report has been formed on the above basis.

Address all mail to: GPO Box 707 CANBERRA ACT 2601
Centenarv House I 9 National Circuit BARTON ACT 2600 Phone (06) 203 7300 Fax (06) 203 7777

Audit Opinion

In accordance with sub section 28(2) of the *Superannuation Act 1990*, I now report that the statements are in agreement with the accounts and records of the Board and, in my opinion:

(i) the statements are based on proper accounts and records;

(ii) the statements present fairly in accordance with applicable Accounting Standards and other mandatory professional reporting requirements the changes in net assets of the PSS for the year ended 30 June 1997 and the net assets of the PSS at that date;

(iii) the receipt of moneys into the Fund, and the payment of moneys out of the Fund and investment of moneys standing to the credit of the Fund, during the year have been in accordance with the *Superannuation Act 1990*; and

(iv) the statements are in the form agreed by the Minister for Finance in accordance with subsection 28(1) of the *Superannuation Act 1990*.

(B) SIS Compliance

Scope

I have conducted tests in accordance with Australian National Audit Office Auditing Standards, which incorporate Australian Auditing Standards, as necessary to provide reasonable assurance as to whether the Superannuation Fund No.1 has complied, in all material respects, with

(a) the relevant requirements of the following provisions (to the extent applicable) of the *Superannuation Industry (Supervision) Act 1993* and Regulations:

Sections 19(2), 19(3), 65, 66, 67, 69-85, 86-93A, 95, 97, 98, 102, 103, 104, 106, 107, 108, 109, 111,112,113,117,118,122,124,125,152,153,154,169;and

Regulations 2.10(1), 2.13(1), 2.21(3), 2.33(2), 2.43(1), 3.10, 4.08(3), 5.08, 9.09, 9.14, 9.29, 9.30, 13.14, 13.17, 13.17A; and

(b) the Guidelines issued by the ISC on Risk Management Statements For Superannuation Entities Investing in Derivatives (to the extent applicable);

for the year ended 30 June 1997.

My procedures included examination, on a test basis, of evidence supporting compliance with those requirements of the *Superannuation Industry (Supervision) Act 1993* and Regulations as specified.

My procedures with respect to the Guidelines consisted of confirming that the relevant Risk Management Statements have been prepared and are broadly consistent with the requirements of the Guidelines. No opinion has been expressed on the appropriateness of the Risk Management Statements or whether the Fund has complied with the procedures set out in the Risk Management Statements.

These tests have not been performed continuously throughout the period, were not designed to detect all instances of non-compliance, and have not covered any other provisions of the *Superannuation Industry (Supervision Act 1993* and Regulations apart from those specified. The Fund's trustees are responsible for ensuring compliance with the requirements of the *Superannuation Industry (Supervision) Act 1993* Regulations and Guidelines.

The opinion on compliance expressed in this report has been formed on the above basis.

Opinion

The Superannuation Fund No. 1, in all material respects, has complied with the requirements of the *Superannuation Industry (Supervision) Act 1993* and Regulations specified above for the year ended 30 June 1997.

Australian National Audit Office

(signed)

Trevor Burgess
Executive Director

For the Auditor-General

Canberra

30 September 1997

Public Sector Superannuation Scheme

Statement by the Trustees of the PSS Fund

The Trustees hereby state that in their opinion:

(a) the attached financial statements of the Public Sector Superannuation Scheme show a true and fair view of the net assets of the Scheme as at 30 June 1997 and the changes in net assets of the Scheme for the year ended 30 June 1997:

(b) at the date of this statement there are reasonable grounds to believe that the Scheme will be able to pay its debts as and when they fall due;

(c) the financial statements are in a form agreed by the Minister for Finance and the PSS Board in accordance with sub-section 28(1)(b) of the Superannuation Act 1990 and have been prepared in accordance with applicable Australian Statements of Accounting Concepts and applicable Australian Accounting Standards; and

(d) the operations of the Fund have been conducted in accordance with the Trust Deed and the Superannuation Act 1990.

Signed at Canberra this 19th day of September 1997 in accordance with a resolution of members of the PSS Board as Trustee of the PSS Fund.

W. Hall
Trustee

J.A. Flitcroft
Trustee

PSS Board

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STATEMENT OF CHANGES IN NET ASSETS FOR THE YEAR ENDED 30 JUNE 1997

	Note	1997 $'000	1996 $'000
Net Assets Available to Pay Benefits at 1 July		**2,076,414**	**1,724,131**
PSS FUND			
Investment Revenue			
Interest		9,589	13,588
Dividends		24,570	21,881
Other Investment Income		71	50
Changes in Net Market Values	2	350,955	121,768
Direct Investment Expenses		(4,279)	(6,612)
		380,906	150,675
General Administration Expenses	1d	(662)	(340)
Net Investment Revenue Before Tax		**380,244**	**150,335**
Contributions Revenue	3a		
Employee Contributions		228,998	191,292
Employer Contributions		112,385	105,685
		341,383	296,977
Benefits Paid	3b	(344,868)	(130,312)
Net Contributions Revenue Before Tax		(3,485)	166,665
Net Investment Revenue and Net Contributions Revenue		376,759	317,000
Income Tax Expense	5	(31,254)	(18,982)
Net Investment Revenue and Net Contributions Revenue After Tax		**345,505**	**298,018**
Add:			
Transfer of Net Assets from the Commonwealth Superannuation Scheme	10	434,851	54,265
Net Investment Revenue and Net Contributions Revenue After Tax and Transfers		**780,356**	**352,283**
CONSOLIDATED REVENUE FUND			
Moneys Appropriated by Parliament	3	760,843	266,535
Less: Benefits Paid	3b	(749,952)	(254,553)
Costs of Administering the PSS Act, Deed and Rules	3c	(10,891)	(11,982)
Net Assets Available to Pay Benefits at 30 June		**2,856,770**	**2,076,414**

The attached notes form part of these financial statements.

STATEMENT OF NET ASSETS
AS AT 30 JUNE 1997

	Note	1997 $'000	1996 $'000
PSS FUND			
Investments	1e		
Short-term Money Market		115,577	75,656
Australian Fixed Interest		76,830	40,850
Australian Equities		726,863	543,996
Units in Commonwealth Funds Management Ltd Pooled Superannuation Trust	4	1,569,289	1,441,172
Other Investments		(22,949)	5,352
Total Investments		**2,465,610**	**2,107,026**
Other Assets			
Amounts due from the Commonwealth Superannuation Scheme	10	434,851	(3,736)
Cash at Bank and on Hand		9,237	8,216
Accrued Income		5,959	3,652
Sundry Debtors		-	877
Future Income Tax Benefit	5	259	-
Total Other Assets		**450,306**	**9,009**
Total PSS Fund Assets		**2,915,916**	**2,116,035**
Less: Liabilities			
Net Outstanding Settlements		730	(7,635)
Sundry Creditors	7	2,519	1,785
Benefits Payable		21,983	24,677
Provision for Income Tax		14,639	14,018
Provision for Deferred Income Tax		19,275	6,776
Total PSS Fund Liabilities		**59,146**	**39,621**
CONSOLIDATED REVENUE FUND			
Other Assets			
Sundry Debtors		40,866	47,547
Total Consolidated Revenue Fund Assets		40,866	47,547
Less: Liabilities			
Benefits Payable		40,866	47,547
Total Consolidated Revenue Fund Liabilities		40,866	47,547
Net Assets Available to Pay Benefits at 30 June		**2,856,770**	**2,076,414**

The attached notes form part of these financial statements.

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NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

For the year ended 30 June 1997

1. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES

(a) *Basis of Preparation*

The form of these financial statements has been agreed by the Minister for Finance and the PSS Board in accordance with sub-section 28(1)(b) of the Superannuation Act 1990.

These financial statements have been prepared in accordance with applicable Australian Statements of Accounting Concepts, applicable Accounting Standards and the Defined Benefit Plan provisions of Australian Accounting Standard (AAS) 25 ' Financial Reporting by Superannuation Plans.

A Defined Benefit Plan refers to a superannuation plan where the amounts to be paid to members on retirement are determined at least in part by a formula based on their years of membership and salary levels.

The Scheme has adopted the provisions of paragraph 22(a) of AAS 25 whereby the financial statements include a Statement of Net Assets, a Statement of Changes in Net Assets and Notes thereto.

Unless otherwise stated, these accounting policies were also adopted in the corresponding preceding reporting period.

(b) *Foreign Currency Translation*

Foreign currency positions are converted to Australian currency using the currency exchange rate in effect at the point of recognition of each transaction. Foreign currency amounts receivable and amounts payable are converted to Australian currency using the exchange rate as at balance date.

(c) *Income Tax*

Income tax has been brought to account using the liability method of tax effect accounting. A provision for deferred income tax has been brought to account in order to recognise the timing effect of income earned during the period that is not assessable for taxation purposes in the current period but is expected to reverse in future periods.

(d) *Expenses of the PSS Board*

In accordance with a determination issued by the Minister for Finance pursuant to section 34 of the Superannuation Act 1990, those costs of the PSS Board which are related to its responsibilities for the management of the PSS Fund and the investment of its moneys are a charge against the Fund. Fees paid to the Chairman of the PSS Board are also a charge against the Fund. All other costs incurred by the PSS Board are paid by ComSuper from moneys appropriated by Parliament.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

For the year ended 30 June 1997

1. SUMMARY OF PRINCIPAL ACCOUNTING POLICIES (continued)

(e) *Valuation of Investments*

Assets of the PSS are recorded at net market value as at the reporting date and changes in the net market value of assets are recognised in the Statement of Changes in Net Assets in the periods in which they occur. Net market values of investments include an amount for selling costs which would be expected to be incurred if the investments were sold.

The bases of market valuations are summarised below.

(i) Short-term Money Market and Fixed Interest - these securities are valued by marking to market using yields supplied by independent valuers.

(ii) Futures Contracts - open futures contracts are revalued to closing price quoted at close of business on 30 June by the Sydney Futures Exchange.

(iii) Equities - listed securities, including listed property trusts, are valued based on the last sale price quoted at close of business on 30 June by the Australian Stock Exchange, or last bid where a sale price is unavailable.

(iv) Exchange Traded Options - options are valued as the premium payable or receivable to close out the contracts at the last buy price quoted at close of business on 30 June by the Australian Stock Exchange.

(v) Overseas Investments - overseas securities are valued on the basis of last sale price quoted at close of business on 30 June by the relevant securities exchange. In the case of UK securities, the basis of valuation is the average of the bid and offer prices.

(vi) CFM Pooled Superannuation Trust (PST) - units in the PST are valued at their net realisable value, which is determined by reference to the net realisable values of units held by the PST in a number of underlying unit trusts. Units in these underlying unit trusts are valued on a basis consistent with the methods listed above that are relevant to the assets held by the underlying unit trusts.

(f) *Use of Derivatives*

The investment fund managers use a number of financial instruments such as futures, options and forward exchange contracts which are known as "derivatives". The objective of their use is to facilitate increases or decreases in exposures in the equity, bond and currency markets consistent with the investment policy of the Fund.

Derivatives are not used for speculation in any of these markets or for the gearing the portfolio.

(g) *Contributions Receivable*

Employee and employer (productivity) contributions are due and payable on each fortnightly contribution day. The contributions do not accrue on a daily basis. Therefore, employee and employer (productivity) contributions in respect of the fortnightly contribution days that fell within the reporting period have been included in the financial statements.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

For the year ended 30 June 1997

2. CHANGES IN NET MARKET VALUES

	1997 $'000	1996 $'000
Changes in Net Market Values of Investments:		
(a) *Investments Held at 30 June*		
Short-term Money Market	405	426
Australian Fixed Interest	1,316	(509)
Australian Equities	119,705	29,770
Currency contracts	(22,818)	-
CFM Pooled Superannuation Trust:		
- CFM International Equities Fund class	170,344	29,450
- CFM Fixed Interest Trust class	15,559	13,633
- CFM Rural Investment Fund class	(546)	1,825
- CFM Property Fund class	4,684	16,527
CFM Australian Equities Fund	8,338	(2,293)
Commonwealth Funds Management Ltd Pooled Superannuation Trust	22,059	(390)
Other Unit Trusts	-	302
	319,046	**88,741**
(b) *Investments Realised During the Period:*		
Short-term Money Market	1,271	2,085
Australian Fixed Interest	2,512	1,160
Australian Equities	15,640	21,920
Currency contracts	11,594	-
CFM Pooled Superannuation Trust:		
- CFM International Equities Fund class	1,400	-
- CFM Fixed Interest Trust class	1,000	7,776
- CFM Rural Investment Fund class	(2,528)	-
- CFM Property Fund class	215	594
CFM Australian Equities Fund	805	(630)
Commonwealth Funds Management Ltd Pooled Superannuation Trust	-	122
	31,909	**33,027**
	350,955	**121,768**

The net loss on foreign currency transactions for the year was $11.224m (1995-96: nil) This amount is the net of the realised and unrealised gains and losses on foreign currency contracts identified above. This does not include gains and losses on foreign currency transactions that may have occurred in the Pooled Trust investments.

3 FUNDING ARRANGEMENTS

(a) *Contributions*

Members contribute to the Scheme at optional rates ranging from a minimum of 2 per cent to a maximum of 10 per cent of salary paid to the member and employers contribute employer (productivity) contributions to the Scheme on a sliding scale averaging 3 percent of salaries paid to the members.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
For the year ended 30 June 1997

3 FUNDING ARRANGEMENTS (continued)

(b) *Benefits*

Where a benefit that becomes payable under the Scheme can be fully met from moneys held in the Fund, the benefit is paid to the beneficiary from the Fund. Where a benefit that becomes payable under the Scheme cannot be fully met from moneys held in the Fund, all moneys held in the Fund in respect of the member are paid into the Consolidated Revenue Fund and the Commonwealth is responsible for the payment of the benefit to the beneficiary from the Consolidated Revenue Fund.

The following provides a breakdown of benefits paid by both the Fund and the Commonwealth:

	1997 $'000	1996 $'000
PSS Fund		
Payments to Commonwealth	303,592	93,347
Lump-sum Benefits	41,276	36,965
	344,868	**130,312**
Consolidated Revenue Fund		
Lump-sum Benefits	712,461	233,636
Transfer Values	3,174	3,219
Pensions	32,968	17,698
Other	1,349	-
	749,952	**254,553**

(c) *Costs of Administration*

The Superannuation Act 1990 requires the Commissioner for Superannuation to provide administrative services to the PSS Board to enable the Board to perform its functions under the Act. The cost of the Commissioner for Superannuation and the staff of ComSuper who assist the Commissioner for Superannuation in the administration of the Superannuation Act 1990 are met from moneys appropriated by Parliament. The amount shown as the Cost of Administering the PSS Act, Trust Deed and Rules in the "Statement of Changes in Net Assets" has been calculated on a full accrual basis.

4. UNITS IN COMMONWEALTH FUNDS MANAGEMENT LTD POOLED SUPERANNUATION TRUST

Class of Unit	1997 $'000	1996 $'000
Australian Equities Fund	28,449	22,838
International Equities Fund	907,715	744,944
Fixed Interest Trust	136,246	172,773
Property Fund	358,817	362,225
Rural Investment Fund	8,193	32,563
Emerging Markets	129,869	105,829
	1,569,289	**1,441,172**

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

For the year ended 30 June 1997

5. INCOME TAX

The taxation liability at 30 June 1997 has been calculated on the basis that the Scheme complies with the standards contained in the Superannuation Industry (Supervision) Act 1993 and Regulations and that tax will be payable at a rate of 15% on net investment earnings, employer contributions and capital gains with deductions allowable for administration expenses.

The aggregate amount of income tax attributable to the period is less than 15 per cent of the Net Investment Revenue and Net Contributions Revenue Before Tax as shown in the Statement of Changes in Net Assets. The difference is reconciled as follows:

	1997 $'000	1996 $'000
Prima facie income tax expense on		
Net Investment Revenue and Net Contributions Revenue Before Tax	56,514	47,550
Add/(Less) Permanent Differences		
Employee contributions	(34,103)	(28,694)
Benefits Paid	51,730	19,547
Income from Pooled Superannuation Trusts	(33,200)	(9,992)
Imputation Credits from Franked Dividends Received	1,516	1,285
Other	(1,102)	(2,068)
	41,355	27,628
Less: Imputation and foreign tax credits	(10,173)	(8,656)
Add: Under provision in prior years	72	10
	31,254	**18,982**

6. SUPERANNUATION CONTRIBUTIONS SURCHARGE

Pending necessary changes to the scheme rules, no provision has been made in these financial statements for the amount of the superannuation contributions surcharge which may be payable under the Superannuation Contributions Surcharge (Assessments and Collection) Act 1997. The Trustees do not anticipate that the superannuation contribution surcharge in respect of 1996-97 will affect the amount of "Net Assets Available to Pay Benefits at 30 June 1997" as disclosed in the financial statements.

7. SUNDRY CREDITORS

	1997 $'000	1996 $'000
Investment Expenses Payable	724	-
Accrued Expenses	295	1,285
Unidentified Contributions	1,175	500
Other	325	-
	2,519	**1,785**

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

For the year ended 30 June 1997

8. AUDITOR'S REMUNERATION

The amount paid and payable in respect of external audit services is $62,500 (1995-96 : $59,500).

9. RESERVE AND DEFERRED LOSSES ACCOUNTS

(a) *Reserve Account*

The income allocation policy provides for the determination of an annual crediting rate. The method for determining the crediting rate involves the transfer of amounts into and out of the Reserve Account. Calculation of the amounts for transfer to and from the Reserve Account for allocation is both a function of the level of income and the level of the Reserve Account as a percentage of the Fund. In general, a higher level of income will tend to result in transfers to the Reserve Account and a relatively high level in the Reserve Account will result in transfers from the Reserve Account. Whilst the current policy does have a smoothing effect on income allocation, its principal purpose is to accumulate adequate reserves which enables the Fund to pursue a more active investment strategy. This has actuarially been estimated to provide higher level returns to members over the longer term.

	1997 $'000	**1996 $'000**
Balance at beginning of year	28,264	10,956
Plus: Transfer from Amount Available for Allocation to Contributors	108,143	16,680
	136,407	27,636
Add: Transfers from the CSS	6,431	628
Balance at end of year	**142,838**	**28,264**

(b) *Deferred Losses Account*

This account exists to provide a mechanism for allocating the loss on revaluation of the assets of the CSS Fund on 1 July 1984 ($215,109,953) to contributors' entitlements. A proportion of the CSS account was transferred to the PSS to recognise that part of the account which related to former members of the CSS who elected to transfer to the PSS:

	1997 $'000	**1996 $'000**
Balance at beginning of year	(6,932)	(8,880)
Add: Transfer from Amount Available for Allocation to Contributors	2,920	2,311
	(4,012)	(6,569)
Less: Transfers from the CSS	(1,829)	(363)
Balance at end of year	**(5,841)**	**(6,932)**

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
For the year ended 30 June 1997

10. TRANSFER OF NET ASSETS FROM THE COMMONWEALTH SUPERANNUATION SCHEME

During the period 1 March to 31 August 1996 members of the CSS were provided with a second opportunity to elect to transfer to the PSS. In addition there was a small number of CSS members returning from leave without pay and invalidity benefits in prior years who had the option of also transferring to the PSS. As at 30 June the Ministerial determinations to effect these transfer had not been completed. Therefore, as at 30 June, the following amounts have been brought to account as current assets of the PSS Fund:

	$'000
Transfer for 2nd Choice campaign	430,845
Transfer for returning members	4,006
	434,851

Since the 30 June, the CSS Board, in agreement with the PSS Board, has made an advance of $423,000,000 to the PSS Board in respect of the assets that are to be transferred to the PSS.

11. VESTED BENEFITS

Vested benefits are benefits which are not conditional upon continued membership of the Scheme (or any other factor other than resignation from the Scheme) and include benefits which members were entitled to receive had they terminated their plan membership as at the reporting date.

The Australian Government Actuary has advised that the estimated amount of vested benefits at 30 June 1997 is $10,000m (1996: $8,000m).

The value of vested benefits has been estimated from the value of vested benefits at 30 June 1996, which was calculated from membership data as at that date, and the trend shown in a projection of accrued benefits made by the Australian Government Actuary as part of an investigation of the scheme during 1996-97. The value of vested benefits could not be calculated from current membership data as at 30 June 1997 as such data was not available.

The value of vested benefits represents the liability that would have fallen on the Scheme if all members had ceased on 30 June 1997 and elected the option which is most costly to the Scheme. The value quoted does not in any way represent the Scheme's liability under circumstances which have any reasonable possibility of arising.

12. LIABILITY FOR ACCRUED BENEFITS

The amount of accrued benefits is the present value of expected future payments which arise from membership of the Scheme up to the measurement date. The accrued benefits are comprised of a funded component, which will be met from the Fund, (ie. accumulated member contributions, and, where applicable, productivity contributions, plus interest) and an unfunded component to be financed from the Consolidated Revenue Fund at the time the superannuation benefits become payable.

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS

For the year ended 30 June 1997

12. LIABILITY FOR ACCRUED BENEFITS (continued)

The amount of accrued benefits in respect of the PSS is calculated on a tri-ennial basis by the Australian Government Actuary. The most recent valuation of the accrued benefits was undertaken by the Australian Government Actuary as part of a comprehensive review during 1996-97 (a copy of the Australian Government Actuary's report is attached).

Accrued Benefits as at 30 June 1996 were:	**$m**
Funded component	2,076
Unfunded component	4,352
	6,428

The movement in the liability for Accrued Benefits since the last actuarial review is:

Balance reported at prior review of 30 June 1993	3,715
Less: Benefits paid	(1,126)
	2,589
Plus: Increase in Accrued benefits	3,839
Balance at 30 June 1996	**6,428**

13. SEGMENT REPORTING

The PSS Scheme operates in the superannuation fund investment industry in Australia however, as part of its investment activities, it also maintains significant overseas investments.

14. RELATED PARTIES

(a) *Trustees*

The Trustee of the PSS, the PSS Board, had the following members during the year:

Mr R.L. Brown (Chairman)
Mr J.A. Flitcroft
Ms W. Hall
Mr K.A. Searson (resigned 14 February 1997)
Mr M.J. Hutchinson (resigned 30 June 1997)
Mr P.G. Skinner (Alternate for Mr K.A. Searson)
Ms S. Wilson (Alternate for Mr M.J. Hutchinson)
Mr J.P. Murphy (Alternate for Mr J.A. Flitcroft)
Mr P.R. Smith (Alternate for Ms W. Hall)

Fees and associated superannuation contributions paid to, or in respect of, those members entitled to receive fees during the year (the Chairman and ACTU nominated trustees) totalled $56,800 (1995-96: fees $48,300).

NOTES TO AND FORMING PART OF THE FINANCIAL STATEMENTS
For the year ended 30 June 1997

14. RELATED PARTIES (continued)

(b) *Associated Entities*

During 1996-97 the CSS and PSS Boards formed a common controlled company, CSS/PSS Pty Ltd for the purpose of taking over trusteeship of the CFM Pooled Superannuation Trust (PST) from Commonwealth Funds Management as of 1 July 1997. As such the Boards have appointed directors, who are current nominated trustees of the CSS and PSS Boards, to manage the company and act as trustees on the transfer of the assets of the CFM PST. Total Risk Management are providing day-to-day administration services for CSS/PSS Pty Ltd. The company was not active during the 1996-97 financial year and is not expected to generate any revenue or costs with costs being paid on an equal basis by the CSS and PSS Funds. As at 30 June the associated entity status between the the PSS and CSS/PSS Pty Ltd was

CSS/PSS Pty Ltd	
Total Shares on Issue	2
PSS Board Shares Held	1
Holding (%)	50%
Total cost incurred by the PSS in relation to the set up of CSS/PSS Pty Ltd and related issues for the period to 30 June 1997	**$37,900**

15. CONTINGENT LIABILITIES

(a) *Investments*

At 30 June the Fund had outstanding investment capital commitments of $22,100,000

(b) *Benefit Entitlements*

In the normal course of business, requests are made by members and former members for the review of decisions relating to benefit entitlements of the Scheme which could result in additional benefits becoming payable in the future. Each request is considered on its merits prior to any benefit becoming payable. In the opinion of the Trustees, these requests do not represent a material liability on the Scheme.

The Trustees are not aware of any other potential contingent liabilities

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PUBLIC SECTOR SUPERANNUATION SCHEME

Accrued Benefits as at 30 June 1996

1. The Australian Government Actuary has been requested by ComSuper to calculate the value of Accrued Benefits for accounting purposes under Australian Accounting Standard 25 (AAS25) as at 30 June 1996 for the Public Sector Superannuation Scheme.

2. The assumptions used to calculate the value of Accrued Benefits were the same as those used by the Australian Government Actuary, Mr C Thorburn, FIAA in his report on the long term cost of the Public Sector Superannuation Scheme and the Commonwealth Superannuation Scheme as at 30 June 1996. A summary of the assumptions and methods adopted in calculating the value of Accrued Benefits is set out in the attached Notes.

3. The value of Accrued Benefits as at 30 June 1996 was $6,428 million. This compares with the value as at 30 June 1993 of $3,715 million.

4. Figures have been calculated in a manner consistent with the Institute of Actuaries of Australia Guidance Note 454.

(signed)

K.E. Deeves
Fellow of the Institute of Actuaries of Australia
Deputy Australian Government Actuary
16 September 1996

INSURANCE AND SUPERANNUATION COMMISSION

Note 1: Summary of Method of Attributing Benefits to Past Membership

Firstly, total benefits payable are projected forward allowing for future salary increases and then discounted back to the valuation date at the valuation rate of interest.

The past membership component for each type of benefit (ie, on retirement, death, disablement or resignation) is then taken to be the proportion of the discounted projected benefit payable on exit that -

- membership completed at the valuation date; bears to
- membership to the projected date of exit

The method used for calculating the past membership component was considered the most appropriate given the nature of the benefit structure of the Scheme.

Note 2: Summary of the Actuarial Assumptions

Financial Assumptions

Discount rate:	7.5% pa
Inflationary salary increases:	5.5% pa
Promotional salary increases:	an age and service related scale was used
Pension increases (CPI):	4% pa

The discount rate has been taken as the long term bond rate as at 30 June 1996 of 8.88% pa, adjusted to take into account investment tax, investment expenses and anticipated future reinvestment rates. The result is rounded to the nearer 0.5%pa.

The weighted average term of the liabilities is considerably in excess of 10 years.

It should be noted that the 2% gap between investment earnings and salary inflation assumed at this review is 0.5% greater than that assumed at the 30 June 1993 review.

The effect of this change has been to reduce the notional employer contribution rate by about 2.2% and the present value of unfunded liabilities by about $2.5 billion from what would have been the case if the 1.5% gap had been retained.

Other Assumptions

Assumptions have been made regarding rates at which in service members will leave the Scheme on account of retirement, death, disablement and resignation. Assumptions were also made about pensioner mortality. These rates have been based on the experience of the Scheme. Full details are set out in the report on the long term cost of the Public Sector Superannuation Scheme and the Commonwealth Superannuation Scheme using data to 30 June 1996.

Reasonableness of Assumptions

Taking into account the circumstances of the Scheme, its membership, assets and benefit structure, I believe the assumptions used are appropriate in relation to the determination of the Present value of Accrued Benefits for the purposes of AAS25.

K E Deeves

16 September 1997

INSURANCE AND SUPERANNUATION COMMISSION

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PUBLIC SECTOR SUPERANNUATION SCHEME

SUMMARY OF THE 1996 LONG TERM COST REPORT

1. A Long Term Cost Report on the Public Sector Superannuation (PSS) scheme and Commonwealth Superannuation Scheme (CSS) was carried out using data as at 30 June 1996 by the Australian Government Actuary, Mr Craig Thorburn, FIAA. This report was presented to Parliament in June 1997.
2. These schemes are partially funded and both schemes have an underlying Government guarantee. Projections of the actual annual employer costs of the two schemes combined (the CSS has been closed to new entrants since July 1990) as a percentage of Gross Domestic Product (GDP) were made over a period of 45 years. These projections showed a progressive fall in costs as the more expensive CSS scheme phased out. The actuary was thus of the opinion that the financial position of the schemes as at 30 June 1996 was satisfactory.
3. The realisable value of assets of the PSS as at 30 June 1996 was $2,076 million.
4. Vested benefits of the PSS were not calculated as part of the Long Term Cost Report as at 30 June 1996 but were calculated separately. They amounted to $9 billion.

   It should be noted that this value of vested benefits represents the liability that would have fallen on the scheme if all members had ceased service on 30 June 1996 and elected the option which is most costly to the scheme. The likelihood of such an occurrence is remote in the extreme. The value quoted does not in any way represent the scheme's liability under circumstances which have any reasonable possibility of arising.

INSURANCE AND SUPERANNUATION COMMISSION

5. The value of Accrued Benefits for the PSS as at 30 June 1996 was $6,428 million. The value of Accrued Benefits is the present value of the proportion of projected future benefit payments that has accrued in respect of membership of the PSS to 30 June 1996.

6. As would be expected in a substantially unfunded arrangement, the value of Accrued Benefits is more than the realisable value of scheme assets at the same date.

7. The report was based on data supplied by ComSuper. In that data, those CSS members who elected to transfer to the PSS during the 1996 period of transfer from the CSS to PSS were recorded as PSS members at 30 June 1996.

8. The major assumptions used in the calculations were as follows:

• Investment earnings rate:	7.5% pa (net of tax and investment expenses)
• Inflationary salary increases:	5.5% pa
• Promotional salary increases:	an age and service related scale was used
• Pension increases (CPI):	4% pa

It should be noted that the 2% gap between investment earnings and salary inflation assumed at this review is 0.5% greater than that assumed at the 30 June 1993 review.

The effect of this change has been to reduce the notional employer contribution rate by about 1.8% and the present value of unfunded liabilities by about $600 million from what would have been the case if the 1.5% gap had been retained.

(signed)

K.E. Deeves
Fellow of the Institute of Actuaries of Australia
Deputy Australian Government Actuary

16 September 1997

INSURANCE AND SUPERANNUATION COMMISSION

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