NSW GOVERNMENT | Treasury

Treasury Circular

TC 18-10
15 June 2018

Accounting for Superannuation

This Circular outlines the accounting treatment for superannuation for NSW public sector entities including Statutory State Owned Corporations for financial years ending on or after 30 June 2018. This Circular withdraws and supersedes the previous circular TC17-07 Accounting for Superannuation.

Summary:

This Treasury Circular outlines the accounting treatment for superannuation for NSW public sector entities, in accordance with Australian Accounting Standards. This Circular applies to NSW public sector entities including Statutory State Owned Corporations (SOCs), for financial years ending on or after 30 June 2018.

This Circular incorporates the additional disclosures based on AASB 1056 *Superannuation Entities* (AASB 1056) effective from FY 2016-17. This Circular mandates certain AASB 1056 disclosures to all NSW public sector entities whose superannuation has not been assumed by the Crown. The main change to this Circular is the change in discount rate for the defined benefit superannuation plan of Statutory SOCs and other for-profit entities from government bond rate to high quality corporate bond rates effective from FY 2017-18.

The accounting treatment for superannuation will vary depending on whether it relates to a defined contribution or defined benefit plan, and whether the defined benefit liability is assumed by the Crown.

This Circular withdraws and supersedes TC17-07 Accounting for Superannuation.

Superannuation balances / funding responsibility assumed by the Crown

The Crown assumes the defined benefit superannuation balances / funding responsibility of certain General Government Sector entities. These entities do not recognise a superannuation liability or asset in their Statement of Financial Position (i.e. as this is recognised by the Crown). These entities are required to recognise a superannuation expense and equivalent revenue for the assumption of the liability.

Superannuation balances / funding responsibility not assumed by the Crown

Where the Crown does not assume the defined benefit superannuation balances / funding responsibility, entities must account for the net defined benefit liability / asset according to AASB 119 *Employee Benefits*.

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1. Background

Accounting for superannuation is outlined in AASB 119 *Employee Benefits* (AASB 119). This Circular incorporates the additional disclosures based on AASB 1056 *Superannuation Entities* (AASB 1056) from FY 2016-17. While AASB 1056 applies only to superannuation entities, disclosure of additional information based on this standard is regarded as providing valuable information. This Circular mandates certain AASB 1056 disclosures to all NSW public sector entities whose superannuation has not been assumed by the Crown. The main change to this Circular is the change in discount rate for the defined benefit superannuation plan of Statutory SOCs and other for-profit entities from the government bond rate to high quality corporate bond rates from FY 2017-18.

AASB 119 describes the accounting treatment for superannuation based upon two classifications: defined benefit plans and defined contribution plans.

In defined contribution plans / schemes, the employer pays fixed contributions (e.g. the superannuation guarantee charge) into a separate entity (a fund). The employer has no legal or constructive obligation to pay any additional contributions (AASB 119, para 8). The employer's expense equals its contributions and the employer's liability is restricted to any outstanding contributions at the end of the reporting period. In NSW, public sector employees who are not members of defined benefit plans / schemes are mostly members of the First State Superannuation Scheme (FSS), which is a defined contribution scheme.

Defined benefit plans are defined in AASB 119, para 8, as plans other than defined contribution plans. In NSW, defined benefit schemes (which are collectively called the Pooled Fund schemes) include the:

- State Authorities Superannuation Scheme;
- State Superannuation Scheme;
- State Authorities Non-Contributory Superannuation Scheme (Basic Benefit);
- Police Superannuation Scheme.

In defined benefit schemes, the formula for calculating the benefit is generally specified in terms of years of service or membership of the fund and final salary or final average salary (over the last three years of service). The future benefits accruing to a member of a defined benefit scheme are the same regardless of the performance of the scheme's invested assets. If investment returns are low, or if gross liabilities increase as a consequence of changes in underlying assumptions in an annual review or an actuarial triennial valuation, the employer may need to increase its superannuation contribution to allow the fund to meet its required benefits (i.e. payouts).

As a result, for defined benefit schemes, a superannuation liability (i.e. excess of gross superannuation liability over the scheme's assets) or prepaid superannuation asset (i.e. excess of scheme's assets over the gross superannuation liability) must be recognised in the Statement of Financial Position by either the Crown or individual entity.

The exact accounting treatment will vary depending on whether or not the defined benefit superannuation balance / funding responsibility is assumed by the Crown.

2. Application

This Circular is issued for financial years ending on or after 30 June 2018. The Circular is issued as a Direction in accordance with sections 9 and 45E of the Public Finance and Audit Act 1983 and applies to all entities required to prepare general purpose financial reports under the Act, including SOCs. A specific reference to the Circular will be included in the Statement of Corporate Intent of SOCs. This Circular withdraws and supersedes TC17-07.

This Circular must be read in conjunction with TC15-07 or its replacement circular regarding personnel service arrangements.

3. Defined Benefit Plans - Crown assumes the superannuation balances / funding responsibility

The Crown assumes the defined benefit superannuation balances / funding responsibility of certain General Government Sector entities.

These entities do not recognise a superannuation asset or liability in their Statement of Financial Position and are not impacted by the AASB 119 requirements. These entities must recognise a notional superannuation expense and equivalent revenue in profit or loss for the assumption of the liability by the Crown, based on certain factors, as outlined in section 3.1 below.

The factors represent an estimate of the contribution the entity would otherwise have had to pay to the superannuation plan to fund the current service cost. This will be calculated differently depending on the particular superannuation scheme.

3.1 Factors for the defined benefit schemes

The following formulae must be used to calculate the superannuation expense and equivalent revenue for the defined benefit schemes to be recognised through profit or loss in the entity's single Statement of Comprehensive Income. The factors shown in the table below were reviewed by the superannuation scheme actuary (Mercer Consulting (Australia Pty Ltd)) and reflect the results of the review of the four superannuation schemes conducted in 2017.

State Superannuation Scheme Actual employee contributions[1] paid to Mercer Administration Services[2] in respect of the financial year.	X	1.0
State Authorities Superannuation Scheme Actual employee contributions paid to Mercer Administration Services in respect of the financial year.	X	1.9
State Authorities Non-Contributory Superannuation Scheme (Basic Benefit) Amount of superable salaries in respect of the financial year (The amount is the figure returned to Mercer Administration Services in terms of s 4 of the State Authorities Non-Contributory Superannuation Act 1987).	X	2.5%
Police Superannuation Scheme Actual employee contributions paid to Mercer Administration Services in respect of the financial year.	X	3.25

Any change in the above factors as compared to the previous financial year should be treated prospectively, as a change in estimate, in accordance with AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors* (AASB 108).

3.2 Disclosure

Disclosure requirements for General Government Sector entities whose superannuation is assumed by the Crown are outlined in the Financial Reporting Code (i.e. they are not subject to the AASB 119 disclosure requirements).

[1] Where employees are contributing on a salary sacrifice basis, the 'employee contribution' refers to the employee contribution *after* the 15% superannuation contribution tax.
[2] Mercer Administration Services (Australia) Pty Ltd

3.3 Payroll tax on superannuation contributions

Payroll tax applies to the payment of employer superannuation contributions in respect of services rendered after 30 June 1996. Where the Crown assumes an entity's superannuation liability, the Crown also assumes the cost of the associated payroll tax. The entity must still recognise the payroll tax expense and the equivalent revenue for the assumption of the liability, by multiplying the superannuation expense by the payroll tax rate for the year.

Regarding Senior Executive officers, entities are responsible in all instances for the payroll tax on that portion of an officer's salary deemed to be employer superannuation contributions by way of salary sacrifice.

4. Defined Benefit Plans - Superannuation balances / funding responsibility not assumed by the Crown

NSW public sector entities whose defined benefit superannuation balances / funding responsibility is not assumed by the Crown must recognise the superannuation expense (or revenue) and any superannuation liabilities / assets in their financial statements, in accordance with AASB 119.

4.1 Superannuation liabilities / assets

In the Statement of Financial Position, entities must recognise the net defined benefit liability (asset), in accordance with AASB 119 (para 8 and 64), as follows:

- present value of the defined benefit obligation;
- less the fair value of plan assets;
- adjusted for any asset ceiling; i.e. present value of economic benefits available as refunds from the plan or reductions in future contributions to the plan.

If an entity has a surplus in a defined benefit plan, it must measure the net defined benefit asset at the lower of the surplus in the defined benefit plan and the asset ceiling (AASB 119, para 64).

Some entities may have a net defined benefit liability for one scheme and prepaid superannuation asset in respect of another. The balances of individual schemes are not to be netted against one another as the conditions for set-off as specified in AASB 119, para 131, will not be met. However, in limited circumstances, if an entity wishes to use a surplus in one scheme to extinguish (fully or partly) the deficit in another scheme, it should seek formal approval from the SAS Trustee Corporation. In some circumstances, this may remove the need for an entity to request a superannuation funding holiday to extinguish a superannuation surplus.

4.2 Defined benefit expense components

Entities must recognise the components of defined benefit expense, except to the extent another Australian Accounting Standard requires or permits their inclusion in the cost of an asset, as follows (AASB 119, para 120):

- Service cost in profit or loss (para 8) – this comprises the current and past service cost and any gain or loss on settlement.
  - Current service cost is the increase in the present value of the defined benefit obligation resulting from employee service in the current period.
  - Past service cost is the change in the present value of the defined benefit obligation for employee service in prior periods from a plan amendment or curtailment.

- Net interest on the net defined benefit liability (asset) in profit or loss (para 8) – this is the change during the period in the net defined benefit liability (asset) that arises from the passage of time.
- Remeasurements of the net defined benefit liability (asset) in other comprehensive income (para 8) – this comprises:
  - actuarial gains and losses – changes in the present value of the defined benefit obligation from experience adjustments (i.e. the effects of differences between previous actuarial assumptions and what actually occurred) and effects of changes in actuarial assumptions, including the discount rate;
  - the return on plan assets (refer definition in AASB 119, para 8), excluding amounts included in net interest on the net defined benefit liability (asset);
  - any change in the effect of the asset ceiling (refer section 4.1), excluding amounts included in net interest on the net defined benefit liability (asset).

4.3 Measurement

The net defined benefit liability / asset recognised in the Statement of Financial Position is determined using an actuarial valuation method, in accordance with AASB 119. This information is calculated centrally and provided to NSW public sector entities by Mercer Administration Services (Australia) Pty Ltd or the Energy Industries Superannuation Scheme (EISS) (using Mercer Consulting (Australia Pty Ltd), the actuary for the State Super Schemes and EISS) in the annual Superannuation Position Statements. Entities must incorporate this information into their financial statements.

AASB 119 requires the inclusion of both employer and employee superannuation assets and liabilities in the calculation of the superannuation liability / asset in their end of year accounts.

A number of actuarial assumptions underlie this calculation including the discount rate, CPI and salary increases. Scheme membership data is also reviewed regularly and takes into account any attrition due to redundancy programmes announced by the State Government.

AASB 119 requires that for not-for-profit public sector entities, the gross defined benefit obligation is discounted based on the long-term government bond rate as at the reporting date (AASB 119, para 83 and Aus83.1). In the case of for-profit entities, the Standard requires that the gross defined benefit obligation is discounted using high quality corporate bond rate, or the government bond rate in the absence of a deep market in high quality corporate bonds (AASB 119, para 83).

NSW Treasury now considers that there is a deep market in high quality corporate bonds in Australia. On this basis, for-profit entities in the NSW public sector must discount using the published yield on high quality corporate bond rates effective from FY17-18. This will also be advised in the annual Superannuation Position Statements.

Note that the change in the basis of the discount rate is considered a change in accounting estimate in accordance with AASB 108. Refer to the Financial Reporting Code for guidance in the financial impact and disclosure requirements.

4.4 Disclosure requirements

This section of the Circular:

- prescribes additional disclosures based on AASB 1056 *Superannuation Entities* (AASB 1056)*;*
- discusses other disclosures arising from AASB 124 *Related Party Disclosures* (AASB 124).

4.4.1 AASB 1056 disclosures

To complement the AASB 119, para 147 requirements regarding the effect of the defined benefit plan on the entity's future cash flows, this Circular requires all NSW public sector entities whose superannuation has not been assumed by the Crown to disclose:

- the surplus or deficit measured as the difference between accrued benefits and the fair value of plan assets determined in accordance with AASB 1056 at the end of each reporting period based on the annual review of the four superannuation schemes;
- current contribution recommendations and whether the actual level of contributions is consistent with the actuary's recommendations;
- qualitative and quantitative information about changes in key components of accrued benefits that provides a basis for understanding the overall change;
- the basis for the assumptions used in the measurement of accrued benefits, including the manner in which they are determined, the key assumptions used, as percentages or in other quantitative terms or in qualitative form, and the sensitivity of the liabilities to reasonably possible changes in key assumptions;
- information about the manner in which the entity manages liquidity risk;
- if applicable, reasons why the actual asset portfolio differs to the asset portfolio used to measure the accrued benefits;
- information explaining any difference between accrued benefits and the fair value of plan assets and the policies for managing such difference, and the anticipated timeline over which the difference is expected to be eliminated;
- where applicable, any plans or processes for the NSW public sector entities to seek repayment of surpluses or reduce future contributions; and
- where relevant, disaggregated financial information where that would help to explain the category of exposed risks.

NSW public sector entities will continue to calculate and disclose information regarding the net defined benefit superannuation liability (or asset) on two bases for:

- recognition in the Statement of Financial Position (i.e. reporting basis) – using the AASB 119 liability discount rate based on the long-term government bond rate for not-for-profit entities and high quality corporate bond rate for for-profit entities as at the reporting date;

- disclosure in the notes to the financial statements (i.e. funding basis) – using the expected rate of after-tax return on plan assets based on the AASB 1056 methodology used by the State Super Schemes and EISS.

The AASB 1056 deficit (surplus) will be lower (higher) than the AASB 119 net defined benefit liability (asset) recognised in the Statement of Financial Position, because the expected after-tax rate of return on plan assets is typically higher than the long-term government bond rate. To help users interpret the financial report this should also be explained in the notes to the financial statements.

The AASB 1056 information is relevant for users of the financial report because it can be used to assess the level of future contributions and reflects the plans' investment strategy as well as the employer's long-term funding plan. It also provides relevant information for other funding decisions including whether or not funds should be transferred between schemes. The above AASB 1056 information, as well as other AASB 119 disclosures, will continue to be provided centrally to NSW public sector entities as part of their annual Superannuation Position Statement issued by Mercer Administration Services (Australia) Pty Ltd or the EISS.

4.4.2 Additional AASB 124 disclosures

Entities may also be required to make additional disclosures where required by AASB 124. This includes disclosures regarding post-employment benefits for key management personnel.

5. Defined Contribution Scheme

The defined contribution is the responsibility of each entity (i.e. the Crown does not assume any asset or liability arising from defined contribution schemes). In the NSW public sector, the First State Superannuation Scheme is the default defined contribution scheme. The accounting treatment for defined contributions is outlined below.

5.1 Superannuation liability / asset

An asset or a liability for a defined contribution scheme is only recognised in the Statement of Financial Position at the end of the reporting period, where there are (AASB 119, para 51(a)):

- prepaid contributions, that will result in a reduction in future payments or cash refund or;
- outstanding contributions for that period.

5.2 Superannuation expense

Under AASB 119, para 51(b), an expense must be recognised for the contribution payable to the defined contribution scheme, for service provided by an employee, except to the extent the amount forms part of the cost of an asset.

For the First State Superannuation Scheme, the superannuation expense is represented by the amount of the superannuation guarantee contribution, which is based on a specified portion of employee's ordinary time earnings. From 1 July 2014, the superannuation guarantee contribution increased to 9.5%. This percentage will increase progressively to 12.00% over a number of years.

5.3 Disclosure requirements

Under AASB 119 para 53, an entity must disclose the amount recognised as an expense for defined contribution plans. Entities may also be required to make additional disclosures, where required by AASB 124. This includes disclosures regarding post-employment benefits for key management personnel.

6. Tax effect of Superannuation

For NSW public sector entities subject to tax under the Income Tax Assessment Act 1936 or the National Tax Equivalent Regime, the tax effect of any superannuation balances (i.e. where superannuation is not assumed by the Crown) must be accounted for under AASB 112 *Income Taxes* (AASB 112). Any superannuation asset or liability recognised in the Statement of Financial Position will give rise to temporary differences under AASB 112. Temporary differences are differences between the carrying amount of an asset or liability in the Statement of Financial Position and its tax base; i.e. which must be accounted for as a deferred tax asset or liability.