



## SUPERANNUATION PRACTICE COMMITTEE

### Information Note: SG Benefit Certificates and salary sacrifice contributions

June 2020

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**A. Purpose and status of Information Note**

1. This Information Note was prepared by the Superannuation Practice Committee ("SPC") of the Actuaries Institute ("Institute") and is intended to:
  - ▶ Ensure actuaries responsible for preparation of Benefit Certificates are aware of recent changes to Superannuation Guarantee legislation regarding the treatment of salary sacrifice superannuation contributions;
  - ▶ Assist actuaries to consider the implications of the legislative changes in preparing Benefit Certificates;
  - ▶ Stimulate Information amongst actuaries of suitable ways of dealing with this issue in the preparation of Benefit Certificates and related advice to clients; and
  - ▶ Encourage feedback to the SPC about appropriate guidance to actuaries, including what amendments should be made to Professional Standard 403.
2. Professional Standard 403 *Preparation of Benefit Certificates* ([PS 403](#)) sets out requirements that actuaries must meet in preparing Benefit Certificates. The SPC is in the process of reviewing PS 403 to take account of the recent legislative changes.
3. This Information Note does not represent a Professional Standard or Practice Guideline of the Institute.
4. This Information Note does not constitute legal advice. Any interpretation or commentary within this Information Note regarding specific legislative or regulatory requirements reflects the expectations of the Institute but does not guarantee compliance under applicable legislation or regulations. Accordingly, Members should seek clarification from the relevant regulator and/or seek legal advice in the event they are unsure or require specific guidance regarding their legal or regulatory obligations.
5. Feedback is encouraged and should be forwarded to the SPC via Paul Shallue ([paul.shallue@mercer.com](mailto:paul.shallue@mercer.com)).
6. This is the first version of this Information Note.

## **B. Introduction**

### **B.1 Recent legislation changes**

7. The *Superannuation Guarantee (Administration) Act 1992* ("the SG Act") was amended in October 2019 'to improve the integrity of the superannuation system by ensuring that an individual's salary sacrifice contributions cannot be used to reduce an employer's minimum superannuation guarantee (SG) contributions'. The amendments apply from 1 January 2020 to:
  - ▶ prevent contributions made under salary sacrifice arrangements from satisfying an employer's SG obligations; and
  - ▶ specifically include salary or wages sacrificed to superannuation in the earnings base for calculating an employer's SG obligations.
8. However, the amendments do not apply to SG obligations met via defined benefit (DB) funds i.e. they only addressed the SG obligations met by contributions made to accumulation funds (or Retirement Savings Accounts).
9. This outcome arises because, under the SG Act, the SG support provided by an employer to a DB fund is required (for both DB and accumulation members) to be assessed and certified by an actuary in a 'Benefit Certificate' prepared in accordance with the SG Act and the associated SG regulations. The provisions in the SG Act and regulations affecting the SG earnings base used for Benefit Certificates were not amended last year when the salary sacrifice changes were made for accumulation funds, nor was there any amendment to prevent salary sacrifice contributions being counted as employer SG contributions in a Benefit Certificate.
10. The ATO has confirmed that the salary sacrifice amendments did not affect the SG provisions regarding the calculation of the SG charge percentage in relation to defined benefit funds, however noted for completeness that in terms of calculating an employer's individual SG shortfall for an employee for a quarter, the employee's salary or wages are effectively grossed-up by the amount of salary sacrifice made by way of a superannuation contribution, so that any charge percentage is applied to the employee's quarterly salary or wages base per that definition in subsection 19(1) of the SG Act. This is the case regardless of the type of fund of which the employee is a member. However, the fact that there is equivalent treatment of the SG charge payable in the event of a shortfall does not resolve the different requirements for meeting SG via a DB fund compared with an accumulation fund.
11. Hence SG legislation results in the following differences from 1 January 2020:

	<b>SG met via DB funds (including Deemed DB funds)</b>	<b>SG met via accumulation funds</b>
SG earnings base	<b>OTE</b> (Ordinary Time Earnings)	<b>OTE Base</b> = OTE plus salary sacrificed super contributions
Employer support for SG	<b>Can include</b> salary sacrificed super contributions	<b>Cannot include</b> salary sacrificed super contributions

## B.2 No change in practice for most employers

12. While the above is the legal position, it is important to note that historically most DB fund employer sponsors have not used salary sacrifice contributions to reduce their SG obligations, with salary sacrifice arrangements designed to provide flexibility to employees without impacting the employer's costs. Applying the new arrangements for accumulation funds to DB funds is highly unlikely to require any change to their practice.
13. However, the SPC also expects that most current Benefit Certificates would not *prevent* an employer from using salary sacrifice contributions to reduce their SG obligations, as:
  - ▶ some current Benefit Certificates may not prevent salary sacrifice contributions from (in effect) being counted as SG contributions; and
  - ▶ most current Benefit Certificates do not ensure salary sacrificed super contributions cannot reduce the SG earnings base.

## C. Implications for Benefit Certificates

### C.1 Review of PS 403

14. As noted earlier, the SPC is considering what action to take regarding PS 403 in response to the recent legislative changes.
15. In considering this issue, it is worth noting that, when announcing the Government's intention to make the salary sacrifice amendments to the SG legislation, the Minister [said](#): *'The Government will seek to legislate a key recommendation of the Superannuation Guarantee Cross-Agency Working Group **to close a loophole that could be used by unscrupulous employers to short-change employees who choose to make salary sacrifice contributions into their superannuation accounts**'* (emphasis added).
16. Therefore, on the one hand, there appears to be no specific legal requirement for PS 403 to be amended to require SG support for Benefit Certificates to be measured against OTE Base (rather than OTE) and to exclude salary sacrifice contributions from being

counted towards an employer's SG obligations. On the other hand, there may be some expectation from outside the actuarial profession that actuaries would close a 'loophole' that may allow an 'unscrupulous' employer sponsor of a DB fund to 'short-change' their employees, even though this is more than the legislation requires.

17. If Benefit Certificates do not prevent an employer from using salary sacrifice contributions to reduce their SG obligations, there remains a risk that members of the relevant funds could be treated less favourably than they would be in an accumulation fund. This may be of concern to some members, trustees and employers and actuaries may be called on to explain why the Benefit Certificate leaves open this possibility, particularly for accumulation section members in a defined benefit arrangement.
18. Whilst acknowledging these potential concerns, the SPC has reservations about amending PS 403 to impose requirements above the legislated minimum for DB funds.

## **C.2 Encouraged approach**

19. **At this stage, the SPC wishes to encourage actuaries to give careful consideration when preparing new Benefit Certificates to:**
  - ▶ **establishing that it is not the employer's practice to use salary sacrifice contributions to reduce their SG obligations; and**
  - ▶ **preparing the new certificate in a manner which reflects the employer's practice and accordingly, as far as practicable, prevents salary sacrifice contributions from reducing the employer's SG obligations.**
20. This would provide clarity that the SG treatment of salary sacrifice contributions is not less favourable to members than is legally required to apply in an accumulation fund (that is not a Deemed DB Fund for SG purposes).
21. It is difficult to envisage circumstances where such an approach would not be supported by an informed employer, for reasons including the following:
  - ▶ It does not seem feasible that an employer would want to provide less favourable treatment of salary sacrifice contributions in its own fund than it would be required to provide where the employee chose another fund. If the treatment is less favourable, this would seem a relevant matter for the employer or the trustee, or both, to disclose to employees/members;
  - ▶ If the employer used salary sacrifice contributions to reduce their SG obligations, an informed employee (who nonetheless wished to remain in the employer fund)

would consider using post tax contributions and claiming a deduction, rather than using salary sacrifice, so the employer would be likely to damage employee relations and the standing of the employer fund while gaining no benefit;

- ▶ A trustee of an accumulation fund is unlikely to agree to the Deemed DB Fund provisions being used to enable SG contributions to be met from reserves if the Benefit Certificate allows less favourable treatment of salary sacrifice contributions than would normally be required;
- ▶ The employer's payroll system would need to cater for two different calculations of the SG earnings base and two different treatments of salary sacrifice contributions; and
- ▶ The employer may suffer reputational damage if it uses a practice which has been characterised by Government as unscrupulous.

### **C.3 Multi-employer DB funds**

22. For multi-employer DB funds it may be difficult for actuaries to establish what the practice is (regarding the SG treatment of salary sacrifice contributions) for all employers. While actuaries will not have relationships with all employers, the Trustee or an employer association may be able to assist, but it is acknowledged that in some cases it may not be practical to determine practice for all employers.
23. One of several possible scenarios where a DB fund Trustee may not have a close relationship with all employers is where the fund has a public offer section. In this situation it is unlikely to be practical to establish the practice of all employers, though clearly any sponsors with which the Trustee does not have a relationship will only be sponsors of accumulation category members and would be unlikely to expect their SG obligations to be any different from those applicable to members of accumulation funds.
24. In such situations it is highly likely that the Trustee will be the client requesting the Benefit Certificate and that the Trustee will consider it appropriate to instruct the actuary to prepare the certificate in a manner that prevents salary sacrifice contributions reducing the SG obligations of the employers covered by it. It is expected that the Trustee would consult with, or inform, the employers about the certificate being prepared on this basis.

### **C.4 Permissible approach**

25. In the unlikely situation that an employer (or Trustee, where applicable) does not request the preparation of a new Benefit Certificate in a manner which, as far as practicable, prevents the relevant employers from using salary sacrifice contributions to reduce their

SG obligations, it is permissible for the Benefit Certificate to be prepared on a basis that does not prevent this.

26. In this situation it would be desirable for the actuary to state prominently in the certificate that it does not prevent the use of salary sacrifice contributions to reduce the employers' SG obligations and, to the extent reasonably practical, set out the reasons why the certificate has been prepared on that basis (for example, in accordance with the instructions of the party requesting the certificate). It would also be preferable for the actuary to add commentary on why treating members of DB funds consistently with accumulation funds is preferred.

### **C.5 Compliance with PS 403**

27. The SPC considers that PS 403 contains sufficient flexibility to allow Benefit Certificates to be prepared in the manner described in paragraph 19 of this Information Note, while still complying with it.
28. In particular, it is permissible for a Minimum Requisite Benefit (MRB) to be higher than the minimum permitted by law. For example:
- ▶ Section 8.5 of PS 403 explicitly allows salary sacrifice contributions to be treated as member contributions rather than employer contributions in the calculation of the MRB and the standard MRBs described in PS 403 provide flexibility for this (it is acknowledged that Section 8.5 will likely require at least contextual updates due to the SG Act changes to the treatment of salary sacrifice contributions for accumulation funds);
  - ▶ The amount of employer contributions required to be included in an accumulation MRB, or used to calculate top-up contributions to an accumulation account where the SG earnings base exceeds DB salary, can be based on OTE Base;
  - ▶ The employer financed portion of a standard DB MRB can be based on average OTE Base, for example refer to Section A1.6(e) of PS 403; and
  - ▶ Where Section 6.7 is used to specify the Notional Employer Contribution Rate (NECR) for an accumulation MRB, usually where the amount of employer contributions actually being made cannot readily be assessed such as may occur in a public offer fund, it would be appropriate to seriously consider specifying that the NECR be calculated by dividing employer contributions by OTE Base (i.e. always giving the same or lower NECR than if dividing by OTE). This would be entirely consistent with the last paragraph of Section 6.7.

### **C.6 Early replacement of existing Benefit Certificates**

29. The SG legislation does not have provisions that enable an actuary to withdraw an existing Benefit Certificate and there is no legislative requirement for the early replacement of existing Benefit Certificates due to the salary sacrifice changes.
30. Nonetheless, a new Benefit Certificate may be issued by the Actuary prior to the expiry of the current certificate if considered appropriate, which will cause the prior certificate to cease to have effect for the period from the effective date of the new certificate.
31. Some trustees and/or employers may request early replacement with a new certificate that provides for salary sacrifice treatment in line with the requirements for members of accumulation funds. Others may be comfortable to let the existing certificate run until its expiry date – in this case it may be desirable to confirm that the employer does not use salary sacrifice contributions to reduce their SG obligations so the trustee can be satisfied it does not have any disclosure obligation that might otherwise apply.

### **D. Conclusion**

32. The SPC acknowledges that actuaries are likely to have a range of views on this matter and that the Benefit Certificate treatment of salary sacrifice contributions needs to have regard to the specific circumstances of each fund.
33. Feedback is encouraged and should be directed to the SPC via Paul Shallue ([paul.shallue@mercer.com](mailto:paul.shallue@mercer.com)). An Insight session will also be held shortly to provide a forum for the exchange of views.

**END OF INFORMATION NOTE**