

Senate Finance and Public Administration Legislation Committee

ANSWERS TO QUESTIONS ON NOTICE

Prime Minister and Cabinet Portfolio

Department of the Prime Minister and Cabinet

Additional Estimates Hearings 2003-2004, 16 February 2004

Question: PM29

Outcome 1, Output 4

Topic: Actuarial advice in relation to Dr Hollingworth

Hansard Page: F&PA 107

Senator Faulkner asked:

Are you able to provide a copy of the actuarial advice?

Answer:

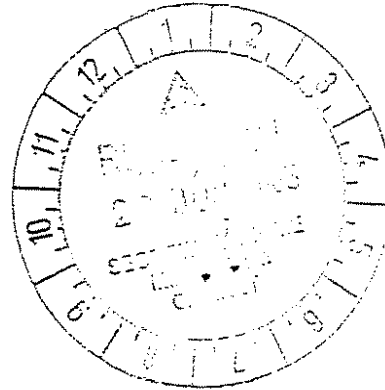
An edited version of the actuarial advice has been provided. The deleted parts of the documents contain personal information regarding Dr Hollingworth, namely the application of the superannuation surcharge to his pension entitlements.

Ref No.:

19 June, 2003

Dr P Shergold
Secretary
Department of Prime Minister and Cabinet
3-5 National Circuit
BARTON ACT 2600

Attention: Ms A Dowd



Dear Dr Shergold

CONVERSION FACTOR FOR DR HOLLINGWORTH - S4(3C) OF THE GOVERNOR GENERAL ACT 1974

Under s4(3C) of the *Governor-General Act 1974* (the Act), you, as the trustee of the Scheme, are required to determine in writing the conversion factor that is applicable for the purpose of working out the yearly amount that would have to be paid to discharge a liability equal to the Governor General's surcharge deduction amount.

Furthermore, s4(3C) provides that your determination must be in accordance with advice received from the Australian Government Actuary.

I therefore recommend that you determine a factor of [REDACTED] as being a conversion factor that is applicable for the purpose of working out the yearly amount that would have to be paid to discharge a liability equal to Dr Hollingworth's surcharge deduction amount.

I have based my recommendation on the following principles, assumptions, and data:

- The transaction is an arms length transaction, neither biased to Dr Hollingworth nor to the Commonwealth.
- The amount of net pension payable to Dr Hollingworth is calculated in accordance with s4 of the Act.
- The real discount rate is 2.5% pa. This assumption is consistent with the economic basis that I have recently adopted in similar contexts.
- Mortality assumptions were those used to value the unfunded liabilities of the Governor-General Scheme as a whole as at 30 June 2002. This, in turn, is the same mortality basis as that used to value the liabilities of the Judge's Pension Scheme as at 30 June 1999.
- Dr Hollingworth's age and his wife's age.

I will write to you separately explaining the effects of the application of s4(3) of the Act on Dr Hollingworth's pension.

Yours sincerely


Peter Martin
Australian Government Actuary

Ref No.:

24 June, 2003

Mr A. Williams
Department of Prime Minister and Cabinet
3-5 National Circuit
BARTON ACT 2600

Dear Mr Williams

GOVERNOR-GENERAL PENSION SCHEME - CALCULATION AND PAYMENT OF NOTIONAL SUPERANNUATION SURCHARGE ACCOUNT IN RESPECT OF DR HOLLINGWORTH

I refer to our recent telephone conversations and am writing to provide further details of the calculation of the notional superannuation surcharge account in respect of Dr Hollingworth and its subsequent payment.

You have informed me that a surcharge assessment in respect of Dr Hollingworth of \$[REDACTED] was issued by the Australian Taxation Office (ATO) to the Scheme in August 2002. As the Governor-General Pension Scheme is an unfunded superannuation scheme, under Section 16 of the *Superannuation Contributions Tax (Assessment and Collection) Act 1997* a (superannuation) surcharge debt account needs to be set up by the Scheme. Interest is added to this account at the end of each Financial Year while the account is in debit. When the benefit becomes payable, the amount in surcharge debt account has to be paid to the ATO within one month of the benefit becoming payable. Dr Hollingworth resigned as Governor-General on 29 May 2003 and I understand that his first pension payment will be on 30 June 2003. Although the legislation is not entirely clear, my understanding is that the balance of the surcharge debt account needs to be paid to the ATO by 31 July 2003.

Although the amount of the notional superannuation surcharge account needs to be paid by 31 July 2003, in practice it should be paid by 30 June 2003 to avoid interest being added to the amount owed to the ATO. If the amount is paid by 30 June 2003, the amount owed to the ATO is \$[REDACTED]. This is because no interest has to be added to the original assessment, as the notional superannuation surcharge account will not be in debit at the end of any Financial Year. If the notional superannuation surcharge account is paid after 30 June 2003, an additional amount of approximately \$[REDACTED] of interest will be payable.

I have been in touch with the ATO and the mechanics of making the payment are as follows:

- The payment should be sent to

Ms Linda Polazzon
Australian Taxation Office
PO Box 277
World Trade Centre
MELBOURNE VIC 8005

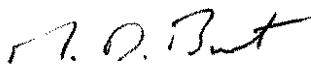
The envelope should be marked 'Private and Confidential'.

- Along with the payment should be an accompanying letter giving
 - Name of Scheme
 - Tax File Number of Scheme
 - Name of the person in respect of whom the payment is being made
 - The amount of the payment
 - Contact details (name, address and telephone number)

In writing this letter, I have assumed that there will be a physical payment made to the ATO. You should note that there may be an alternative way of discharging the Scheme's taxation obligation. This would be by way of a determination made by the Minister of Finance under Section 6 of the *Superannuation Contributions Tax (Application to the Commonwealth) Act 1997*. You should bear in mind that the alternative appears to operate entirely at the discretion of the Minister of Finance. If you do use this alternative, it would be desirable to inform the ATO of this.

Should you have any queries on this matter please contact me on (02) 6263 4126.

Yours sincerely



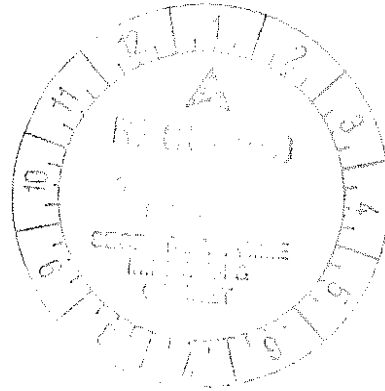
Michael Burt
Actuary

Ref No.:

25 June, 2003

Dr P. Shergold
Secretary
Department of Prime Minister and Cabinet
3-5 National Circuit
BARTON ACT 2600

URGENT



→ Attention: Mr A. Williams

Dear Dr Shergold

GOVERNOR-GENERAL PENSION SCHEME - DR HOLLINGWORTH'S PRESCRIBED PERCENTAGE EXPLANATION

I recently wrote to you recommending a conversion factor of [REDACTED] for Dr Hollingworth. When this is applied to Dr Hollingworth's benefits it results in a prescribed percentage of [REDACTED]%. This represents a [REDACTED]% reduction in the full rate pension due to the superannuation surcharge. This is significantly less than the 15% (top superannuation surcharge tax rate) reduction which at first sight might have been expected. I am writing to provide an explanation for the difference.

There are three major factors which have played a part in this outcome. They are:

- Earlier than expected retirement

Dr Hollingworth left Office after just less than two years. The notional employer contribution figure reported to the Australian Taxation Office (ATO) was calculated on the basis he would be in Office for five years. As he has retired earlier than expected, he will receive the pension for longer and hence have a more valuable benefit than expected. This is beneficial to Dr Hollingworth as the surcharge debt is deducted from a more valuable benefit, leading to a smaller effective reduction.

- Different actuarial bases (economic assumptions)

The actuarial basis underlying the calculation of amounts to be reported to the ATO is prescribed in the legislation. In providing a recommendation on the conversion factor, I have used what I consider to be more realistic economic assumptions. Again this results in a reduction in the effective rate of surcharge from 15%.

- No interest added to the ATO assessment

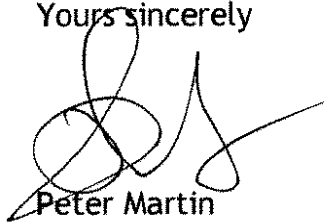
There are inherent timing lags in the ATO assessment process. This is due to the fact that contributions are not reported until after the end of the financial year

and then need to be matched up with an individual's taxation return before an assessment can be issued. In Dr Hollingworth's case, these lags resulted in no interest being added to the ATO assessment. Again this results in a reduction in the effective rate of surcharge.

The three factors mentioned have, very roughly, the same order of impact.

Should you have any queries on this matter please contact me on (02) 6263 4127.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Peter Martin', written over the typed name.

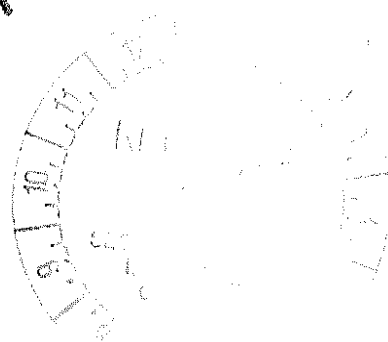
Peter Martin
Australian Government Actuary

Ref No.:

25 June, 2003

Dr P Shergold
~~Secretary~~
Department of Prime Minister and Cabinet
3-5 National Circuit
BARTON ACT 2600

URGENT



→ Attention: Mr A. Williams

Dear Dr Shergold

GOVERNOR-GENERAL PENSION SCHEME - DR HOLLINGWORTH'S BENEFITS

I am writing to give a summary of Dr Hollingworth's benefits from the Governor-General Pension Scheme.

I set out the relevant information below:

Data

Dr Hollingworth's date of birth	10 April 1935
Mrs Hollingworth's date of birth	19 May 1936
Date of exit from Office	29 May 2003
Chief Justice salary at 29.5.03	\$308,100

Surcharge Debt Account

In the case of an unfunded defined benefits superannuation scheme, under Section 16 of *Superannuation Contributions Tax (Assessment and Collection) Act 1997*, the scheme is required to keep a surcharge debt account for each member of the scheme. When a benefit becomes payable to a member, the scheme must discharge its taxation obligation in respect of this member. Interest is added to the account at the end of each financial year while the account is in debit.

The (superannuation) surcharge debt account in respect of Dr Hollingworth is calculated as follows:

	\$
Initial surcharge assessment (August 2002)	
Interest	0.00
Closing debt account (paid June 2003)	

No interest was added to the account as it was not in debit at the end of any financial year.

Calculation of Benefits under Section 4 of the Governor-General Act 1974

Subsection (3)(a) is the relevant section as the surcharge debt account was in debit on 29 May 2003. The allowance payable is the greater of 85% and the prescribed percentage, of the basic rate. The calculation of these figures are set out below:

- *Basic Rate (Section 2A(2))*

The basic rate is the full rate of allowance that would be paid if the surcharge debt account were zero. This is 60% of the salary payable to the Chief Justice of Australia.

This is

$$60\% \text{ of } \$308,100 = \$184,860$$

- *Prescribed Percentage (Section 4 (3B))*

The trustee of the scheme (Secretary of the Department of Prime Minister and Cabinet) has made a determination under Section 4(3C) that the conversion factor is 16.491.

The surcharge adjustment (SA_1) under Section 4(3B) is calculated as follows:

$$\frac{\text{Surcharge debt account}}{\text{Conversion factor}} = \frac{\text{[REDACTED]}}{\text{[REDACTED]}} = \text{[REDACTED]}$$

Conceptually, this can be thought of as the initial reduction in pension due to the superannuation surcharge.

The prescribed percentage is now calculated as follows:

$$\left[1 - \frac{SA_1}{\text{Basic rate}} \right] = \left[1 - \frac{\text{[REDACTED]}}{\text{[REDACTED]}} \right]$$

$$= \text{[REDACTED]\%}$$

This is the prescribed percentage.

As the prescribed percentage is greater than 85%, this is the figure that applies for the purposes of calculating benefits.

- *Initial pension amount payable*

At 29 May 2003, the rate of allowance payable to Dr Hollingworth is:

$$\text{[REDACTED]\% of 60\% of the salary paid to the Chief Justice of Australia}$$

$$= \text{[REDACTED]} \times .60 \times 308,100 = \$\text{[REDACTED]} \text{ per annum}$$

Summary of Benefits

The allowance payable to Dr Hollingworth is:

██████% of 60% of the salary paid to the Chief Justice of Australia.

At 29 May 2003, this amounted to \$██████ per annum.

A reversionary benefit is payable to Mrs Hollingworth, should Dr Hollingworth predecease her of:

62.5% of ██████% of 60% of the salary paid to the Chief Justice of Australia.

At 29 May 2003, this amounted to \$██████ per annum.

I suggest that you may want to provide a copy of this letter to Dr Hollingworth for his records.

If you have any queries on this matter please contact me on (02) 6263 4126.

Yours sincerely



Michael Burt
Actuary