

**Private and Confidential**

## **Report to the Trustee**

# **Actuarial Investigation of the Financial Condition of AvSuper Fund (under SPS 160)**

**as at 30 June 2022**

Prepared by



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**Fellow of The Institute of Actuaries of Australia**

Date: 15 December 2022

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## **Section 1 – Summary**

### **1.1 Background**

#### ***Nature of the Advice***

This report has been requested by Nick Smith, Executive Manager – Finance & Risk AvSuper Fund. In this report, AvSuper Fund is referred to as the “Fund”.

The trustee of the Fund is AvSuper Pty Ltd. In this report, AvSuper Pty Ltd is referred to as the “Trustee”.

I have provided the advice in the report in my capacity as Actuary (as defined in the trust deed) to the Fund. Further explanation on my advice can be obtained using the contact details set out on the first page of the report.

The advice is provided to the Trustee only and may be inappropriate for any other party to use as the basis of any action or decision it takes.

The previous valuation was carried out as at 30 June 2019 by Jeff Humphreys of CHR Consulting Pty Ltd. The report on that valuation was dated 19 November 2019.

#### ***Fund Background***

The trust deed governing the Fund is dated 20 December 2012.

The Principal Employer is Airservices Australia. The Associated Employers is Civil Aviation Safety Authority. The term “Employer” is used throughout this document and should be read as both the Principal Employer and the Associated Employers or only the Principal Employer depending on the context in which it is used.

The Fund is open to new members. However, the defined benefit category was closed in 2002.

The Fund is a complying superannuation fund and is taxed at the rate of 15% (nil for pension assets).

Under the trust deed:

- Each Employer must contribute to the Fund the amount or rate of contributions determined by the Principal Employer from time to time after obtaining the advice of the Actuary and consulting the Trustee.
- If the contributions being made and expected to be made to the Fund and the actual and expected assets of the Fund are together inadequate to provide for the actual and expected liabilities of the Fund the Trustee may adjust members’ benefits.

***Compliance***

The report satisfies the requirements of APRA's Prudential Standard SPS 160.

The report complies with Professional Standard 400 of The Institute of Actuaries of Australia.

***Purpose***

The major purposes of this report are to:

- Examine the adequacy of the assets to meet the liabilities;
- Advise the Trustee on a suitable minimum Employer contribution rate;
- Review the investment policy and the insurance arrangements.

This report is provided triennially. In addition to this report, the Trustee receives actuarial and other advice on a regular and frequent basis to assist it to monitor the financial position of the Fund. Annual actuarial advice on the financial position of the Fund is included as a component of the Fund's risk management strategy.

**1.2 Financial Position of the Fund**

The Fund's financial position was very healthy at 30 June 2022:

- There was an excess of assets over the Actuarial Value of Accrued Benefits, in respect of defined benefit liabilities, the margin being 44% of the value of the benefits. See Section 6.6.
- The Fund was in a Satisfactory Financial Position with a ratio of assets to Vested Benefits (amount of benefits payable if all members left the Fund) of 110% and a ratio of 143% in relation to the amount of the defined benefit vested benefits and defined benefit assets. See Section 5.1.

The significant features of the experience (see Section 1.4 below) that have affected the financial position of the Fund are:

- the investment performance relative to the rate of increase in salaries (the real rate of return) which was lower than expected at the last valuation; and
- The reduction in the number of defined benefit members at a time when the Fund has an excess of assets over liabilities.

Overall, the experience has had a positive impact on the short term and long term financial position of the Fund. Sections 5 and 6 of the report set out in detail the financial position of the Fund.

### 1.3 Employer Contribution Rate

#### (a) Current Rate

Over the 3 years to 30 June 2022, the Employers contributed in respect of Defined Benefit members at the following rates:

| Employer    | Employer Contribution Rate<br>(% of Salaries) |          |     |
|-------------|---|----------|-----|
|             | Full Non<br>ATC                               | Full ATC | CSS |
| Airservices | 0.0   |          | 3.0 |
| Other       | 0.0   | n/a      | 3.0 |

The Employer contribution holiday for Full members commenced with effect from 1 July 2018.

#### (b) Recommended Future Contribution Rate

The Trust Deed sets out the process for determining the contributions to the Fund. It is the responsibility of the Employer to decide the appropriate level of contributions, after receiving the advice of the Actuary and consulting the Trustee.

The recommendations in this report in relation to contributions are made only for the Trustee and should assist the Trustee in this consultation process. Our recommendations therefore are minimum contribution recommendations for the circumstance of the Fund at this time.

There are many considerations in relation to an appropriate future contribution rate and these are set out in Section 7.2.

Taking these considerations into account, my recommendation is that the current contribution rate of 3% for CSS members and nil for Full members can be maintained until the next valuation (as at 30 June 2025). It is likely that at this point contributions will again be required from the Employer. Based on the assumptions in this valuation, a rate of around 5% of salaries is expected.

#### ***Summary of Recommended Rates***

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AvSuper SIS Valuation as at 30 June 2022

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The recommended minimum Employer contribution rates from 1 July 2022 are set out in the table below.

| <b>Employer Contribution Rate<br/>(% of Salaries)</b> |            |
|---|------------|
| <b>Full</b>   | <b>CSS</b> |
| 0.0   | 3.0        |

^ subject to review at the time of completion

Salary sacrifice member contributions are made by the Employer for some employees and the member contribution rate is increased by 17.6% to allow for the taxation of these contributions.

In addition, the Employer is contributing at the rate agreed in respect of Accumulation members.

#### **1.4 Experience**

The significant items of experience during the three years ended 30 June 2022 were:

- a) The defined benefit membership fell over the last 3 years from 838 to 508;
- b) The average rate of increase in members' salaries over the 3 years was 2.9% p.a., which was similar to the previous three-year period and slightly lower than that expected at the previous valuation, an average of 3.5% p.a. – See Section 2.4;
- c) The investment return, net of fees and taxes on the defined benefit assets was 2.6% p.a., significantly lower than the assumed rate, 4% p.a.. See Section 3.2; and
- d) The real rate of return was -0.4% p.a. which was lower than the assumed rate. See Section 3.3.

#### **1.5 Insurance Arrangements**

The Fund does not self-insure.

##### ***Insurer***

The Fund's insurer over most of the period since the last valuation was Hannover Life Re of Australasia Ltd.. The Fund changed insurers from 1 April 2022 to AIA Australia Limited.

***Insurance of the Defined Benefit Liability***

The Fund insures the future service component of the death and TPD benefit and the whole of the Temporary Disability Income Benefit for Full members. The future service component for Full members is:

$$20\% \times \text{Salary} \times \text{Future membership to age 60}$$

This is appropriate while the value of the assets is at or around the amount of vested benefits but should be reviewed if assets become out of line with vested benefits.

The future service component for CSS members is nil.

***Insurance for Accumulation Members***

Accumulation members who are employees of the Employer receive cover at the level of Full members.

Members who leave the Employer and retain their membership of the Fund have their cover maintained at the level that applied at the time of exit. Members may apply for additional death, TPD and IP cover and may opt out of cover.

***Conclusion***

The insurance arrangements are appropriate to the circumstances of the Fund.

**1.6 Investment Policy**

Overall, the investment policy of the Fund is appropriate to the nature of the Fund's design and liabilities.

The Employer has committed to supporting the Fund with additional contributions in those times where short term investment performance deteriorates, and this results in members' minimum benefit entitlements not being fully covered by the assets.

**1.7 Sensitivity Analysis**

Sensitivity analyses have been undertaken in relation to the material risks set out in Section 1.9 a) and b). These form part of Sections 5 and 6.

**1.8 Material Risks**

The material risks for the Fund are:

- a) The rate of investment return relative to the rate of salary increase is lower than that expected over the long term. This will most likely mean that the contribution rate will have to be increased, though not necessarily in the short term.
- b) Short term investment return volatility (down) associated with the current state of the world economy The Fund has a significant asset buffer and has put in place a more defensive asset structure. It is therefore in a reasonable position to absorb poor (relative to that expected in this report) investment performance.
- c) The Employer withdraws its support to make additional contributions.
- d) A downturn in the Australian or international economy to the extent this impacts investment returns at the same time it impacts the Employer's ability or willingness to make necessary topup contributions.
- e) Regulatory and policy risks. These are numerous, examples include:
  - the effect of continually increasing regulatory and accounting rules and oversight making the costs of running the Fund prohibitive or uncompetitive; and
  - the effect of changes to the rules relating to superannuation or retirement incomes policy which increase the rate of exit of members particularly if the Fund is in an unsatisfactory financial position at that time.

The material risks are primarily associated with the investment outlook.

## **1.9 Previous Recommendations**

The Trustee has addressed all the recommendations made in the Previous Report.

## **1.10 Next Valuation**

The next actuarial valuation of the Fund is required by the SIS Regulations and the trust deed to be carried out no later than as at 30 June 2025.

## **1.11 Recommendations**

Recommendations are made in this report in relation to the contribution rate in Section 1.3 above.

No other recommendations are made.



## Section 2 - Membership Data and Experience

### 2.1 Category Definitions

The following category definitions are used for the purpose of this report.

**Corporate Member** - A member of the Fund who is an employee of an Employer and for whom the Employer is contributing. The Corporate member categories are:

- Full Member – a person admitted to the Fund under Section 1.15.2 (b) of the Trust Deed who is accruing a defined benefit under Division 2 of the Trust Deed.
- CSS Member - a person admitted to the Fund under Section 1.15.2 (a) of the Trust Deed who is accruing a defined benefit under Division 2 of the Trust Deed and who is also a member of the Commonwealth Superannuation Scheme (CSS).
- Accumulation Member - a person admitted to the Fund under Section 1.15.6 who is accruing an accumulation benefit under Division 4 of the Trust Deed.

**Public Offer Member** - A member of one of the following categories:

- Deferred Benefit Member - has ceased to be an employee of the Employer and who has elected to retain all or part of his or her benefit within the Fund under Division 3 of the Trust Deed.
- Spouse Member – a person who is the spouse of an existing member, who is not an employee of the Employer and who joins the Fund under Division 5 of the Trust deed.
- Family Law Member – a person who has become a member under a family law benefit split.
- Public Offer Member – a person who joins the Fund under Division 6 of the Trust deed, including other standard employer sponsored members.

**Income Stream Member** – a member who has elected to receive all or part of his or her benefit as an income stream under Division 3 of the Trust Deed.

**Defined Benefit Member** - A Full member or a CSS member.

A member may be in more than one category.

## **2.2 Membership Data**

The membership data has been provided by the Fund's administrator, Mercer.

### ***Data Integrity***

Membership data is unaudited.

We have undertaken reasonableness checks on the data in respect of defined benefit members and we are satisfied with its accuracy for the purposes of this report.

We have not undertaken additional reasonableness checks on the data in relation to accumulation accounts.

### ***Data Summary***

At 30 June 2022 there were:

- 5,835 members of whom 508 were defined benefit members; and
- the vested benefits of all members as shown in the accounts totalled \$2,091m.

## **2.3 Significant Features of the Membership Experience**

### ***Defined Benefit – Full Members***

The Full member category is the key driver of the financial position of the Fund. Movements in other membership categories are not material to the financial position.

Full members exited at relatively high rates, around 15% p.a. over the period since the last valuation, mainly driven by the continuing restructure of the Airservices workforce and poor publicity from APRA's investment performance test.

The number of Full members at the valuation date was 501, down from 785 at the last valuation.

## **2.4 Salary Escalation**

The rate of salary escalation for Defined Benefit members has a direct effect on the liabilities of the Fund. Salaries increased at a rate of 2.9% p.a. over the 3 years ended 30 June 2022. This was similar to the prior 3 year period, 2.8% p.a.. It was slightly lower than the assumed rate at the previous valuation, 3.5% p.a..

Looking forward, it is reasonable to expect that:

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AvSuper SIS Valuation as at 30 June 2022

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- the salary increase rate for the defined benefit category will in general be lower than for all employees of the Employer. This is because the closure of the category to new members removes, over time, the experience of younger members who are expected to have the highest percentage promotional increases; and
- general salary increase rates will increase with the return of higher inflation and a more proportional share of productivity improvements going to the household sector of the economy.

## **Section 3 – Fund Accounts, Asset Values and Earning Rates**

### **3.1 Fund Accounts and Asset Valuation**

The Fund accounts as at 30 June 2022 were produced by the Fund’s administrator, Mercer. The accounts are audited.

The accounts show that the value of the assets of the Fund at 30 June 2022 was \$2,326,502,502.

The assets that are available to meet the liabilities of the Fund after excluding the amount held to meet the Operational Risk Financial Requirement and the Other Reserve was \$2,300,425,803.

The reserves are established by the Trustee as part of the prudent management of the Fund. Their purpose is to pay for contingent short-term liabilities (less than 12 months) and unplanned expenses which may relate to projects, increased regulatory requirements and other matters as part of the operation of the Fund and to provide funding for operational risk events where losses may arise relating to the Fund.

The assets have reduced by 5% since the last valuation.

The value of the Assets adopted for the purposes of the short term and the long term valuation, the determination of the contribution rate recommendations and the Funding Status Measures is \$2,300,425,803.

The accounts also set out the amount held with each investment manager and within each major asset sector.

### **3.2 Investment Return on Defined Benefit Assets**

The rate of investment return on the defined benefit assets is derived from the movement in the unit price of the Defined Benefit investment option over the period plus the administration asset fee (ranged from 0.19% p.a. to 0.23% p.a. over the period) which is charged through the unit pricing process.

The rate of return on the defined benefit assets over the 3 years since the last valuation is set out in the table below:

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| Year ended<br>30 June | Rate of<br>Return<br>(% p.a.) |
|-----------------------|-------------------------------|
| 2020                  | -1.3                          |
| 2021                  | 11.2                          |
| 2022                  | -1.7                          |
| <b>Average</b>        | <b>2.6</b>                    |

The average return of 2.6% p.a. was lower than the prior 3 year period, 6.1% p.a.. It was lower than that assumed at the previous valuation, 4.0% p.a.. The rates were heavily impacted by the economic effects of the Pandemic.

### 3.3 Real Rate of Return

The real rate of return on the Fund's defined benefit assets is the excess of the rate of return over the rate of increase in salaries of defined benefit members. This is one of the critical factors in the determination of the required contribution rate (see also Section 6.5).

The real rate of return for the three years ending 30 June 2022 was -0.4% p.a. which is much lower than the prior period, 3.2% p.a., and slightly lower than that assumed at the last valuation, 0.3% p.a..

The real return over the period has had a negative impact on the financial position of the Fund.

### 3.4 Investment Policy

#### ***Background***

The Fund has an investment strategy, which is set out in the Investment Governance Framework Policy (the Policy) dated May 2022.

The Policy is reviewed at least annually by the Trustee and is currently under review.

The Policy includes amongst other things:

- the investment philosophy and objectives of each section of the Fund;
- the strategy for achieving these objectives; and
- the procedure adopted for the monitoring of the performance of the Fund's investments.

The Investment objectives of the Defined Benefit Section are:

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- To achieve a return after tax and fees that exceeds Average Weekly Ordinary Times Earnings (AWOTE) increases by at least 1.5% pa over rolling 10 year periods;
- To outperform the return of the 'benchmark' portfolio after fees and tax over rolling 10 year periods; and
- To achieve no more than 3 negative annual returns in every 10-year period.

Since the last valuation, the Trustee has made minor changes to the equity sectors. It has also introduced a new sector, the DB Sector. The DB Sector is designed to rebalance the DB Option through overlays to the desired strategic asset allocation and can also include investments that apply to the DB from time to time, being aware of the long term objectives of this Option. Investments in the DB Sector include cash, derivative overlays, investment grade global fixed interest securities which includes corporate securities/bonds, mortgage securities, macro and credit strategies.

The overall structure has not changed significantly, and this can be seen in the table below.

| Sector                   | 30 June 2019  |                       | 30 June 2022  |                       |
|--------------------------|---------------|-----------------------|---------------|-----------------------|
|                          | Benchmark (%) | Range Above/Below (%) | Benchmark (%) | Range Above/Below (%) |
| Australian Equities      | 15            | +15 -10               | 13.5          | +26.5 -8.5            |
| Overseas Equities        | 15            | +15 -10               | 16.5          | +13.5 -11.5           |
| Real Assets              | 17            | +13 -17               | 17            | +13 -17               |
| Private Markets          | 5             | +5 -5                 | 5             | +5 -5                 |
| <b>Total Growth</b>      | <b>52</b>     | <b>+13 -26</b>        | <b>52</b>     | <b>+13 -27</b>        |
| DB Sector                | n/a           | n/a                   | 0             | +50                   |
| Diversified Fixed Income | 20            | +20 -20               | 20            | +20 -20               |
| Cash                     | 20            | +15 -5                | 20            | +20 -20               |
| Alternatives             | 8             | +32 -8                | 8             | +32 - 8               |
| <b>Total Defensive</b>   | <b>48</b>     | <b>+27 - 13</b>       | <b>48</b>     | <b>+27 -13</b>        |
| <b>Total</b>             | <b>100</b>    |                       | <b>100</b>    |                       |

The defined benefit liabilities of the Fund are approximately 23% (down from 31%) of total liabilities which is a large reduction since the last valuation. The defined benefit liabilities remain a significant feature of the Fund. However, the proportion is expected to continue its

long term path of reduction as defined benefit members continue to exit the Fund and a large proportion retain their benefit within the accumulation options provided by the Fund.

The unit pricing reports set out the amount held with each investment manager and within each major asset sector.

The investment policy is discussed below.

### ***Nature of the Liabilities – Defined Benefit***

The average term of the defined benefit liabilities is 8 years, which is unchanged from the prior valuation.

The average age of defined benefit members in the Full category is 54 (last report 53) and the average period of employment is 28 years (last report 26 years). The average age has not increased to the extent expected as retrenchment programs generally see a higher proportion of older members leave than younger members.

Full members exited at a high rate, around 15% p.a.. This reflected the retrenchment programs over the period. A larger proportion of members are approaching retirement ages and it is expected that the underlying exit rate, which is around 6%, will increase over time.

The liabilities are “real” i.e., will vary with movements in salaries. The defined benefit assets should include exposure to those asset sectors that include a high likelihood of positive real returns over the long term. These assets are generally considered to be equities (listed and unlisted, property and infrastructure) as the growth in salaries is determined to a significant extent by the inflation rate and GDP growth, both of which impact on dividends and the value of the assets.

The Fund has a healthy buffer (allowing for a payment of Surplus assets to the Employer) and can afford to bear some short term fluctuations in investment returns from equities while the liabilities remain long term and the Employer is able to meet short term additional contributions when necessary. The Employer has shown that it is willing to do this when required.

### ***Defined Benefit Liquidity***

The defined benefit section of the Fund is cashflow negative with the Employer on a contribution holiday. This is exacerbated by:

- Recent poorly performing investment markets so investment returns are not supporting the cashflow position; and
- The likely payment of Surplus Assets (as defined in the Trust Deed) to the Employer in 2023.

The combination of these events puts pressure on the asset allocation of the defined benefit assets. The Trustee is managing this situation with the assistance of the asset consultant, Frontier.

***Defined Benefit Investment Strategy***

The Trustee has a conservative investment strategy. This reflects the shortening term of the liabilities, as well as the decision to secure the strong financial position of the Fund by reducing the exposure to growth asset sectors.

The current investment policy reflects the nature of the liabilities.

***Nature of the Liabilities – Accumulation***

A growing proportion of the liabilities of the Fund is in respect of members with accumulation accounts including defined benefit members. From 1 October 2002, these members have had investment choice and the members effectively determine their own investment strategy from the options provided by the Trustee. The Trustee's focus here is on providing an appropriate range of choice and appropriate investment managers within each investment option.

Members are advised in the Fund's communication material about the nature of each investment choice option.

The MySuper investment option holds most of the accumulation account liabilities and this is expected to continue.

Investment earnings are credited using a daily unit pricing mechanism which allows for taxation and expenses. This crediting rate strategy is appropriate for the Fund.

***Liquidity***

The Fund is managing short term liquidity issues associated with a series of independent factors that impact monies flowing into the Fund, including:

- the defined benefit issues as outlined above;
- the impact of the YFYS legislation on new member flows; and
- the impact of the APRA investment performance test, a test that is not fit for purpose but was nevertheless imposed on the industry by the regulator. AvSuper was required to advise members it failed APRA's test, and this led to a higher than usual loss of members.

The Fund has predominantly investments with short redemption notice periods.



The Fund carries no self-insurance for death and TPD benefits.

Longer term, liquidity issues will become significant as the current generation of defined benefit members starts to draw down from the retirement and rollover products.

### ***Diversification***

The investments are appropriately diversified, spreading risk across asset sectors, within sectors and by investment style of manager. This will assist in reducing short term fluctuations in returns.

### ***Defined Benefit Margin Policy***

The Trustee has in place a policy in respect of the margin of assets over defined benefit liabilities. The policy is:

- The Trustee has set a Target Margin of 10% of assets over vested benefits in relation to Defined Benefit liabilities.
- The Trustee generally monitors movements in the margin of assets over vested benefits annually. The Trustee will advise the Principal Employer when it becomes aware that the margin of assets over vested benefits has fallen below the Target Margin and will raise the potential for the Employer to make additional contributions if deemed appropriate.

The margin of 10% provides a good buffer for the expected level of asset fluctuation inherent in the current investment policy. When considered together with the commitment to additional funding made by the Employer, this reserving policy is suitable for the Fund's circumstances.

## **3.5 Previous Recommendations**

We made no recommendations in our last report regarding the Investment Policy of the Fund.

## **3.5 Conclusion**

Overall, the current Investment Policy and the management of the short term liquidity issues are appropriate to the nature of the Fund's design and liabilities.

## **Section 4 – Valuation Method and Assumptions**

### **4.1 Method**

The Fund's design is such that the valuation must be considered on two levels:

#### ***Short Term Solvency***

The assets of the Fund should be sufficient to cover vested benefits so that:

- Members benefits are fully funded if the Employer ceased contributions, the Fund was to windup or undergo a major membership loss;
- To the extent possible, the Defined Benefit Margin is maintained; and
- the Fund's financial position is not unsatisfactory under the SIS Act.

The valuation must therefore take into account the likely progression of the assets and vested benefits over the short term. We have used a period of 5 years to examine the progression. The method used to examine the short term solvency is to project the assets and vested benefits ignoring membership movements (which make little difference to the results). Appropriate allowance is made for administration, insurance and tax costs.

The method used is the same as that used in last year's report.

#### ***Long Term Viability***

The long term viability of the Fund is examined to ensure sufficient assets are being accumulated to meet the long term benefit commitments, under the Fund's design, on an ongoing basis. The Attained Age Normal Method is used to estimate the required Employer contribution rate in respect of the future service liability of existing members. It also estimates the amount of any excess of assets over past service liabilities.

The method is the same as that used at the previous valuation except that members aged 65 and over are valued in the same way as all other members rather than at their vested benefit.

### **4.2 Assumptions – Short Term Solvency**

The critical factors affecting short term solvency assuming a return to normal member defined benefit exit rates are:

- the margin of investment returns over the salary increase rate, the real rate of return; and
- the Employer contribution rate.

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Assumptions based on expected short term experience have been adopted. These are varied to examine the sensitivity of the short term position to the experience. The assumptions used are set out below:

- Average Salary increase 4.8% p.a. (previously 3.5% p.a.) including a full allowance for the effect of promotional and terms of employment changes. The salary increase rate is reasonably stable and variations in this assumption are not considered necessary for the projections.
- Investment return assumptions are net of tax and investment expenses. The underlying investment assumptions over the year ended 30 June 2023 are:
  - Rate earned to 31 October 2022 is approximately 1.1%;
  - Long term corporate bond rates, 5% p.a.;
  - Real assets, Private and Alternatives as set out in the Investment Governance Framework Policy.

The most volatile investment sector, listed shares, is likely to have the greatest effect on the year's return. The assumed capital gain in share values and return on the defined benefit assets for the year ended 30 June 2023 are set out below.

I have also shown the Surplus Assets payment to the Employer under each scenario. This payment is the amount estimated at the date of payment so that the Total Fund Value is equal to the Total Accrued Benefit Value at that date.

| Scenario | Capital Gain in Share Portfolio * (%) | All Ordinaries Index 30 June 2023 | Return for the year (%) | Surplus Assets (\$m) |
|----------|---------------------------------------|-----------------------------------|-------------------------|----------------------|
| A        | -25%                                  | 5290                              | -3.0                    | 32                   |
| B        | -20%                                  | 5640                              | -1.4                    | 43                   |
| C        | -10%                                  | 6350                              | 1.7                     | 64                   |
| D        | 0%                                    | 7055                              | 5.2                     | 88                   |
| E        | 10%                                   | 7760                              | 7.3                     | 102                  |

\* from 1 November 2022 to 30 June 2023

The All Ordinaries Index is shown to give some context to the estimated investment return. The All Ordinaries Index as at 31 October 2022 was approximately 7,055.

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AvSuper SIS Valuation as at 30 June 2022

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This assumption looks primarily at the downside risk for the Fund with the current economic outlook highly unstable and uncertain.

The investment return net of tax and investment expenses in years 2, 3, 4 and 5 is assumed to be 5.3% p.a., being the assumed long term rate.

- The Employer contributes at the current rates. For those members where the Employer makes the member contribution, the member contribution rate is increased by 17.6%;
- Administration expenses are 0.19% p.a. of assets. Investment expenses are accounted for in the investment return assumption. Group life premiums are around \$0.3m p.a. in respect of the defined benefit death, TPD and TTD benefits.
- Surplus Assets are returned to the Employer during the year ended 30 June 2023. The amount is \$111m as at 30 June 2022 reduced so that at the date of payment the Total Fund Value does not become less than the Total Accrued Benefit Value. The reduction, if any, will reflect any lower than required investment return over the period from 1 July 2022 to the payment date and the impact of the contribution holiday over the period from 1 July 2022 to the date of payment. The return required for a payment of \$111m is 8.5% p.a. to the date of payment.

The investment assumptions have been changed from those used at the previous valuation to reflect the current economic outlook for the Fund. Salary escalation is increased from 3.5% p.a. at the last valuation to 4.8% p.a..

#### **4.3 Assumptions – Long Term Viability**

The valuation assumptions are based on best estimate long term expectations. The assumptions used are summarised below:

##### ***Key Financial Assumptions***

- Salary increase rate, 4.8% p.a. (last valuation 3.5% p.a.);
- Earning rate after tax and investment fees on defined benefit assets, 5.3% p.a. (last valuation 4.0% p.a.); and
- Average real return 0.5% p.a., unchanged from the last valuation.

##### ***Salary Increase Rate***

The salary increase assumption is set after:

- detailed discussion with the Employer;

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- detailed analysis of the salary experience of the Employer, particularly in relation to promotional increases;
- consideration of economic forecasts; and
- analysis of financial market indicators, particularly in relation to expected long term inflation rates.

The salary increase assumption is consistent with the current underlying economic fundamentals inherent in the investment earning rate assumption as well as past salary experience and takes into account expected salary increases due to promotion and the industrial agreements in place or expected to be in place between employees and the Employer in the future.

The salary assumption is the sum of the future long term expected:

- Inflation rate;
- General salary increases in the economy;
- Additional salary increases reflecting the circumstances of Airservices; and
- Promotional salary increases, both through progression scales and through role changes.

The assumption is higher than at the last valuation, reflecting the increase in the current and expected inflation rate.

***Investment Returns***

The long term investment return is assumed to be 5.3% p.a..

The Trustee's objective for investment returns is 1.5% above wage growth (AWOTE only). This is consistent with the assumed return as the salary promotional effect is significant and does not form part of the trustee's objective.

The Trustee's investment return objective is consistent with current long term economic fundamentals, including the inflation rate, risk free rate and the equity risk premium. A rate of 5.3% p.a. is consistent with these fundamentals when applied to the defined benefit asset mix.

The assumption is higher than at the last valuation, 4.0% p.a., reflecting the increase in inflation rates and bond rates over the period which are expected to remain at higher rates compared with the past 10 years.

***Other Assumptions***

- The share of the administration expenses of running the Fund for defined benefit members will be 0.19% p.a. of defined benefit assets. Assuming the Target Margin is maintained on average over the long term, this equates to 0.21% p.a. of liabilities. In addition, all members with accumulation accounts will be charged fees on a fair cost recovery basis.
- Employer contributions will be taxed at 15%. For those members where the Employer makes the member contribution, the member contribution rate is increased by 17.6%;
- Rates of decrement as set out below. The decrement rate due to retrenchment is assumed to be nil; and

| Age    | Death/TPD |        | Resignation and Retirement |        |
|--------|-----------|--------|----------------------------|--------|
|        | Male      | Female | Full                       | CSS    |
| 30     | 3         | 2      | 500                        | 500    |
| 35     | 4         | 3      | 280                        | 280    |
| 40     | 6         | 5      | 230                        | 230    |
| 45     | 10        | 8      | 180                        | 180    |
| 50     | 18        | 15     | 200                        | 200    |
| 55     | 31        | 26     | 416                        | 3,290  |
| 56–59* | 40        | 31     | 583                        | 2,782  |
| 60     | n/a       | n/a    | 1,690                      | 1,800  |
| 61–64* | n/a       | n/a    | 1,764                      | 1,800  |
| 65     | n/a       | n/a    | 2,222                      | 1,800  |
| 70     | n/a       | n/a    | 1,960                      | 1,960  |
| 75     | n/a       | n/a    | 4,460                      | 4,460  |
| 79     | n/a       | n/a    | 10,000                     | 10,000 |

\* average over the age group

- The employer is on the contribution holiday for Full members for the whole of the projection period.

The Other Assumptions, apart from the contribution holiday, are unchanged from the last valuation.

The decrement experience is hard to determine after the restructures of recent years particularly the restructure in 2016/17. These have an impact both in the year of the restructure and the immediately following years. A decrement experience analysis will be undertaken by the time of the next valuation.

## Section 5 – Results: Short Term Funding

### 5.1 Short Term Funding Status Measures

#### *Vested Benefits*

The ratio of the Fund's assets to vested benefits (VBI) is set out in the tables below:

At 30 June 2022 the Fund was not in an Unsatisfactory Financial Position with the ratio of assets to vested benefits being greater than 100%.

| Fund as a Whole       |                            | Ratio of Assets to Vested Benefits at 30 June (%) |      |
|-----------------------|----------------------------|---|------|
| Value of Assets (\$m) | Value of Liabilities (\$m) | 2019  | 2022 |
| 2,300                 | 2,091                      | 110   | 110  |

| Defined Benefit Liabilities Only |                            | Ratio of Assets to Vested Benefits at 30 June (%) |      |
|----------------------------------|----------------------------|---|------|
| Value of Assets (\$m)            | Value of Liabilities (\$m) | 2019  | 2022 |
| 700                              | 491                        | 132   | 143  |

The vested benefit is the benefit the member is entitled to under the Trust Deed on exit. For defined benefit members, this is the Retirement benefit for those eligible (by age) and the Resignation benefit for all others. With the closure of the Fund to new members, the Retirement benefit and Resignation benefit are equal for all members.

For Public Offer, Income Stream and Accumulation members, the vested benefit is the value of their account balance.

The ratios show the short term position of the Fund if all members exited or there was a large reduction in membership.

The defined benefit ratio indicates that the Fund's financial position has improved over the 3 years. This was due principally to the reduction in the number of defined benefit members while the fund has had an excess of assets over vested benefits.

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AvSuper SIS Valuation as at 30 June 2022

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The Trustee's Target Margin is a defined benefit vested benefits ratio of 110% and the Fund sits comfortably above this margin.

***Minimum Benefits***

The Minimum benefit is the Minimum Requisite Benefit (as defined in the Benefit Certificate) in accordance with the Superannuation guarantee legislation. The Minimum Benefit for all members is in the nature of an accumulation benefit.

The value of the liabilities of the Fund in respect of the Minimum Benefits of the members of the Fund was \$1,991,841,762.

The ratio of the Fund's assets to the Minimum Benefits in relation to defined benefit members only is set out in the table below:

| <b>Defined Benefit Members Only</b> |                                   | <b>Ratio of Assets to Minimum Benefits at 30 June 2022 (%)</b> |
|-------------------------------------|-----------------------------------|--|
| <b>Value of Assets (\$m)</b>        | <b>Value of Liabilities (\$m)</b> |  |
| 700                                 | 352                               | 199  |

The ratio is very healthy with Minimum Benefits very well covered by the assets. As all Minimum Benefits are in the nature of accumulation benefits, this ratio is expected to remain strong provided the minimum contributions set out in the funding and Solvency Certificate are made by the Employer. A payment of Surplus Assets to the Employer will reduce this ratio but it will remain very healthy.

The Fund is used to meet obligations under the Superannuation Guarantee Administration Act 1992. All necessary funding and solvency certificates were obtained during the three-year period to 30 June 2022. The current Funding and Solvency certificate was issued with effect from 1 July 2022 and was dated 28 September 2022.

An actuary is highly likely to be able to certify the solvency of the Fund in any Funding and Solvency Certificate that may be required over the three years commencing 1 July 2022.

**5.2 Projection of Defined Benefit Vested Benefits Ratio**

The projection is for 5 years based on short term realistic assumptions set out in Section 4.2. For the purpose of the projection, the value of the accumulation benefits has been taken from both the value of vested benefits and the value of the assets as these liabilities are fully matched by the assets (liabilities move in proportion to investment returns).



## AvSuper SIS Valuation as at 30 June 2022

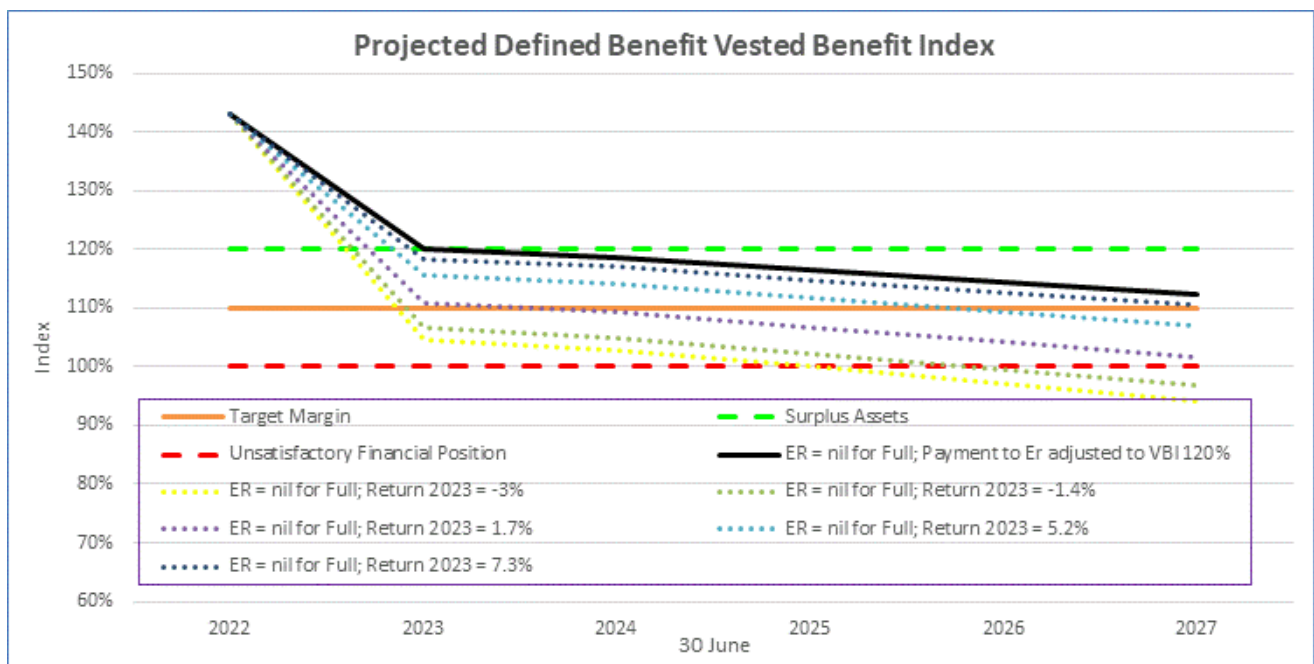
The projection therefore shows the effect on the margin of assets over vested benefits for those benefits independent of investment returns and dependent on salary changes. The experience in relation to these benefits is the major risk to the Fund of failing the Satisfactory Financial Position test.

The results of the projections are set out in the graph below. The graph shows the defined benefit VBI at the end of each year through to 30 June 2027 based on the scenarios set out in Section 4.2.

The graph includes the Trustee's Target Margin (VBI = 110%), the Surplus Assets margin (VBI = 120%) and the Unsatisfactory Financial Position (VBI = 100%).

The result is the black line and is the same for all scenarios as the Surplus Asset payment to the Employer is adjusted to 120%, at the time of payment, absorbing the impact of the lower than required investment return to 30 June 2023. The required investment return for a Surplus Asset payment to the Employer of \$111m is 8.5% p.a..

The dotted projections show the impact on the financial position if a payment of \$111m was made to the Employer under each of the short term investment return assumptions.



The significant conclusions arising from the projections are:

- a) The Trustee's Target Margin of 10% is highly likely to be exceeded through to 30 June 2023.

- b) The VBI is expected to fall gradually after payment of Surplus assets to the Employer.
- c) Based on these projection assumptions, the buffer above the Target Margin is expected to fall to a point where the Employer will need to start to contribute again for Full members in the medium term.

### 5.3 Fund Wind-Up

On Fund wind up, or if the Employer ceases to contribute at sufficient rates, the assets are apportioned among the members. There are no underlying guarantees of benefits. The funding method aims to ensure that the value of accrued benefits or vested benefits if greater is covered by the assets at all times.

If the Fund winds up and members are compulsorily transferred to a new superannuation fund, the member's Fund Interest (as defined in the Trust Deed) is transferred to the new fund. In the circumstances of the Fund (Fund Assets exceeding the value of benefits) the Fund Interest is:

**“the value.....of the benefits presently and prospectively payable from the Fund to and in respect of that person to the extent that those benefits have accrued....”**

This can be taken to be approximately the Actuarial Value of Accrued Benefits as shown in Section 6. The coverage of the Wind-Up benefits is therefore the same as the coverage shown in Section 6.

## **Section 6 – Results: Long Term Funding**

### **6.1 Introduction**

The Fund's long term financial position and Employer contribution rate are examined in this Section.

The liabilities have been valued using the assumptions set out in Section 4.3. The funding method used is the Attained Age Normal method. Under this method the normal Employer rate is calculated as sufficient on a best estimate assumption basis to finance future service liabilities of existing members.

The best estimate assumption basis is set using assumptions which:

- a) are made using professional judgement, training and experience;
- b) are made having regard to relevant statistics, experience and other information; and
- c) are neither deliberately overstated nor deliberately understated.

The best estimate assumptions should be viewed as coming from a range of best estimate assumptions rather than as a single correct number, this being the nature of these estimates.

The results of the valuation using these assumptions are expected to be equally likely to overstate as understate the actual cost of the benefits. Sensitivity analysis is used to quantify the effect of the actual experience moving away from that expected.

The assets have been valued in Section 3.

### **6.2 Normal Employer Contribution Rate for Existing Full Members**

The Normal Employer contribution rate is the level rate required, based on the valuation assumptions, to fund the benefit liabilities accruing in respect of members' future service with the Employer.

The valuation produced a normal Employer contribution rate for existing Full members of 13.9% of salaries of these members.

In addition, the Employer contribution rate for CSS members is 3% of the salaries of these members.

The valuation results are set out below:

AvSuper SIS Valuation as at 30 June 2022

|  |                | \$                     |
|--|----------------|------------------------|
| Value of Future Service Liabilities                                |                | <b>163,380,114</b>     |
| Value of Future Contributions                                      | Member         | 51,976,818             |
|  | CSS Employer * | 128,257                |
| Value of net Future Service Liability of Full Members              |                | <b>111,275,039</b>     |
| Value of 1% of salaries of Full members                            |                | <b>9,422,191</b>       |
|  |                | <b>(% of salaries)</b> |
| Employer Contribution Rate after expenses and before tax           |                | 11.8                   |
| Tax on Employer contributions                                      |                | 2.1                    |
| <b>Required Normal Employer contribution rate for Full members</b> |                | <b>13.9</b>            |

\* at 3% of salaries for these members less tax

The required rate disclosed in the calculation has fallen slightly since the last valuation (14.5% of salaries).

### 6.3 Assets and Past Service Liabilities (Actuarial Value of Accrued Benefits)

The valuation shows that the value of the assets exceeds the value of past service liabilities by \$214m. The Fund is in a strong financial position.

The excess has reduced since the last valuation which showed an excess of assets over liabilities of \$240m.

The results are set out below:

|   | \$                   |
|---|----------------------|
| Value of DB Past Service Liabilities for DB Members less Surcharge Accounts | 486,105,209          |
| Value of accumulation accounts of all members                               | 1,599,954,487        |
| <b>Total Past Service Liability</b>   | <b>2,086,059,696</b> |
| <b>Value of Assets</b>  | <b>2,300,425,803</b> |
| <b>Excess of the Value of Assets over Past Service Liabilities</b>          | <b>214,366,107</b>   |

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AvSuper SIS Valuation as at 30 June 2022

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At the valuation date, the value of the assets of the Fund is adequate to meet the liabilities in respect of the accrued benefits of the members of the Fund.

#### **6.4 Employer Contribution Rate for Future New Full Members**

The long term rate of Employer contribution for new entrants is no longer relevant as the Fund has been closed to new Full members.

#### **6.5 Variation in Assumptions**

The major determinant of the adequacy of the assets of the Fund and the stability of the required Employer contribution rate is the extent to which the rate of return on the Fund's assets exceeds the rate of increase in salaries. This is referred to as the real rate of return for the Fund. The valuation assumes the real rate of return will be 0.5% p.a..

The effect of a 0.5% p.a. reduction in the real rate of return is to:

- increase the normal rate by around 0.6% of salaries (to 14.5% of salaries); and
- reduce the excess of assets over past service liabilities by \$22m, from \$214m to \$192m.

The variation is shown to provide an understanding of the effect of an actual outcome that varies from the expected. It does not imply that this is a likely result or a lower bound on the possible actual investment return of the Fund over the long term.

#### **6.6 Long Term Funding Status Measure – Actuarial Value of Accrued Benefits**

The ratio of the Fund's assets to the Actuarial Value of Accrued Benefits is set out in the tables below:

| Fund as a Whole       |                            | Ratio of Assets to Actuarial Value of Accrued Benefits at 30 June (%) |      |
|-----------------------|----------------------------|---|------|
| Value of Assets (\$m) | Value of Liabilities (\$m) | 2019  | 2022 |
| 2,300                 | 2,086                      | 111   | 110  |

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AvSuper SIS Valuation as at 30 June 2022

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| <b>Defined Benefit Liabilities Only</b> |                                   | <b>Ratio of Assets to Actuarial Value of Accrued Benefits at 30 June (%)</b> |             |
|---|-----------------------------------|--|-------------|
| <b>Value of Assets (\$m)</b>            | <b>Value of Liabilities (\$m)</b> | <b>2019</b>  | <b>2022</b> |
| 700                                     | 486                               | 136  | 144         |

The Actuarial Value of Accrued Benefits is set out in Section 6.3.

The ratio of assets to the Actuarial Value of Accrued Benefits has increased since the last valuation. The Fund's experience has had a positive impact on the financial position, particularly the membership reduction. The ratio is very healthy and indicates the Fund is in a very strong financial position.

## **6.7 Shortfall Limit**

The Trustee's Shortfall Limit is 95%. The Shortfall Limit is appropriate for the Fund in its circumstances.

## **Section 7 – Future Employer Contributions**

### **7.1 Introduction**

This Section sets out the significant considerations in determining the recommended minimum Employer contribution rate as set out in Section 1.3.

### **7.2 Recommended Contribution Rate - Considerations**

The following considerations should be taken into account when determining the overall minimum Employer contribution rate:

- i) The Trust Deed requires the Employer to determine the contribution rate, after obtaining the advice of the Actuary and consulting the Trustee.
- ii) The financial position of the Fund is strong (Section 5 and 6) with a healthy level of reserves relative to the current investment policy. The Fund can withstand large falls in share values and still retain the Trustee's Target Margin of 110%. This allows for a smooth and orderly reintroduction of Employer contributions.
- iii) Around 75% of the total liability of defined benefit members is funded.
- iv) The Employer is likely to need to start contributions again from 1 July 2025 albeit at a low rate. For example, a rate of 5% of salaries would allow a gradual reduction in the VBI to the Target Margin of 110% by 2033 based on the valuation assumptions.
- v) The Employer has made a long term commitment to funding any shortfalls in assets over appropriate periods of time. This considerably enhances members' security and provides very good underlying support to the investment strategy of the Trustee.
- vi) The Trustee receives annual advice from the Actuary on the financial condition of the Fund as well as internal monthly monitoring of the vested benefits ratio. This allows the Trustee to react quickly to any change in circumstances, including discussing the contribution rate with the Employer.
- vii) There is small risk in the short term that the financial position will deteriorate to an extent where contributions would need to be made quickly.
  - o Salary growth is stable and low and presents no risk.
  - o The investment strategy is conservative, and this protects the Fund to an extent against fluctuations in growth sector asset values particularly listed shares.

## **Attachment A – Summary of Fund Provisions – Defined Benefit Members**

### **A.1 Eligibility**

Employees became members of the Fund from the first day of service.

Employees who are members of the CSS are eligible for award benefits only.

### **A.2 Contributions**

Full members may contribute at the rate of 0% to 10% of salary, in whole multiples. The rate may be varied at any time during the year.

Salary means salary at the date of the member's last birthday.

CSS members do not contribute to the Fund.

The Employer contributes at the rates necessary to finance the balance of the cost of benefits and running the Fund.

### **A.3 General Benefit Provisions**

Air Traffic Controllers and Flight Information Service Officers may retire from age 50. Other members may retire from age 55.

The general benefit formula is:

$$\{\text{Accrued Benefit Multiple}\} \text{ times } \{\text{Final Average Salary}\}$$

where:

- Accrued Benefit Multiple is the sum of the individual benefit accruals over the relevant periods of membership and any multiple for previous fund membership. The benefit accrual rates are set out in Section A.4. Part time employees receive a prorata accrual rate.

For death and TPD before age 60 for Full members, the Accrued Benefit Multiple is the multiple that would have accrued at age 60.

For resignation for Full members, the Accrued Benefit Multiple is reduced in the first 4 years of membership by a vesting scale (Section A.6).

- Final Average Salary is the average of the member's salary on the 3 birthdays preceding exit date. For part time employees, the equivalent full time salary is used.



Where a Surcharge liability arises in respect of a member, the amount is accumulated at the Fund earning rate and deducted from the member's benefit on exit.

All benefits are subject to the minimum amount required to comply with the Superannuation Guarantee legislation.

#### **A.4 Retirement and Retrenchment Benefit**

For Full members, the accrual rate depends on:

- The current rate of member contribution; and
- The average rate of contribution since joining the Fund.

This is shown in the following table:

| Member Contribution Rate<br>(% of salary) | Benefit Accrual Rate (%)  |  |
|---|---|--|
|   | Standard<br>(average member contribution rate since joining more than 5%) | Catchup<br>(average member contribution rate since joining less than 5%) |
| 0   | 10.0  |  |
| 1   | 12.0  |  |
| 2   | 14.0  |  |
| 3   | 16.0  |  |
| 4   | 18.0  |  |
| 5   | 20.0  |  |
| 6   | 21.2  | 22.0   |
| 7   | 22.4  | 24.0   |
| 8   | 23.6  | 26.0   |
| 9   | 24.8  | 28.0   |
| 10  | 26.0  | 30.0   |

The accrual rate for CSS members is 3% p.a.

#### **A.5 Death and TPD Benefit**

For Full members before age 60, the death and TPD benefit is increased by 20% for each year from the date of exit to age 60. For CSS members the benefit is the accrued retirement benefit.

#### **A.6 Resignation Benefit**

For Full members in the first 4 years of membership, a vesting scale applies to the difference between the multiple accrued in respect of membership of the Fund and the vested benefit multiple (the average member contribution rate plus 3%, times years of membership). The vesting scale is 25% for each year of membership. Part years count proportionately after the first year. For all other members the benefit is the accrued retirement benefit.

Currently vesting does not apply as all members have more than 4 years of membership in the Fund.