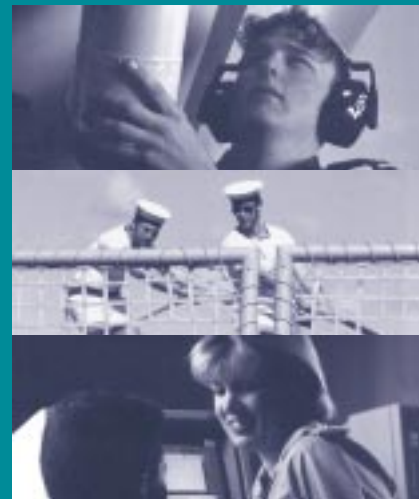


MSBS

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A N N U A L R E P O R T T O M E M B E R S FROM THE MILITARY SUPERANNUATION AND BENEFITS BOARD OF TRUSTEES

FUND PERFORMANCE

OBJECTIVE

The Fund's primary investment objective is to achieve a return of 5% per annum above inflation (after tax, investment fees and other expenses) over the long term, that is rolling five to seven year time periods.

PERFORMANCE

Over the past three years, the Fund remains ahead of its objective of beating inflation by an average of 5% per annum over the long term. This performance was achieved despite bad investment markets in 1994. Fortunately, these investment markets have changed in early 1995.

The table below shows the Fund's returns for the three years to 30 June 1995 (after tax and fees). Inflation for the same periods is included, so that annual real growth in Fund earnings is shown. The Fund has performed broadly in line with the industry average over the past three years.

MSB FUND PERFORMANCE (AFTER TAX AND FEES) TO 30 JUNE

	1992-1993 %	1993-1994 %	1994-1995 %
MSB Fund	12.5	7.2	6.4
Inflation (CPI)	2.7	1.7	4.5
Real return	9.8	5.5	1.9

The chart, 'MSB Fund Performance' on page 2, illustrates how \$1000 invested at the inception of the Fund would have grown at the Fund earning rate compared to the growth in inflation since September 1991.

The Trustees have been reviewing the investment strategy of the Fund with the aim of achieving an after tax and fees return of 5% per annum above inflation over rolling five to seven year time periods.

THE 1994-95 CREDITING RATE

With every superannuation contribution you make, your stake in the Fund grows and that stake grows further every year as it earns interest. Each year, the Board declares an annual **crediting rate** of interest that is credited to your accumulated contributions for the financial year just completed.

Did you know that beating inflation by 5% per annum would mean that your money buys -

70% (or 1.7 times) more in 10 years,

and

550% (or 5.5 times) more in 35 years

The crediting rate for the year is 5.8%. The earnings rate of the MSB Fund for 1994-95 is 6.4% (after tax and management fees). This result is equivalent to the average returns earned by similar accumulation funds.

The annual crediting rate for the past three years is as follows:

The annual crediting rate for 1992-93 was 12.1%

The annual crediting rate for 1993-94 was 5.4%

The annual crediting rate for 1994-95 was 5.8% ▶

► The methodology for the calculation of the annual crediting rate and exit rate is likely to change following the review of the Board's investment policy being undertaken by IPAC, the Fund investment adviser. Further details will be included in the new Investment Policy Statement which is currently being refined. Members will be informed once the statement becomes available.

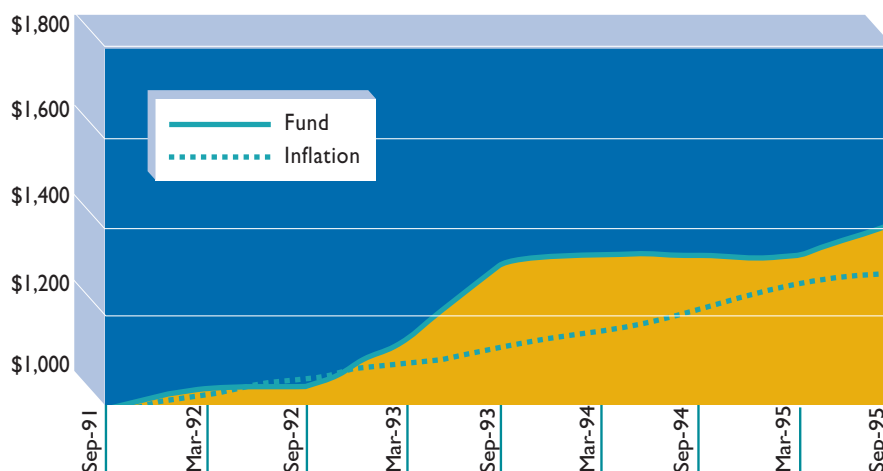
The *earnings rate* and the *crediting rate* differ because they reflect different aspects of the Fund. The earnings rate reflects Fund investment performance for the year (after tax and management fees); while the crediting rate reflects how much can be credited to members' accounts, given Fund size, growth from investment and cash flows, such as benefits paid and

► contributions received. For 1994–95, the crediting rate also had to be adjusted to allow for the overestimation of the earnings rate in the previous year (See page 7).

FEES AND CHARGES

The amount available for distribution to members represents the net income and other expenses directly related to the operation of the Fund. The administrative costs in respect of the operations of ComSuper are met from Budget appropriations and are not a charge against the Fund.

MSB FUND PERFORMANCE



INTEREST RATES

Early in each financial year, the Trustees determine a rate of interest to be applied to contributions held in each member's accumulation account at 30 June. This rate of interest, which is determined only once each year and is known as the *crediting rate*, is based on the earnings received on the Fund's investments over the previous financial year. The crediting rate for 1994–95 is 5.8% (effective from 1 July 1995). The crediting rate is shown on your member information statement.

A rate of interest, known as the *exit rate*, is applied to the contributions of members leaving the Scheme to cover

► the period between the last crediting rate and their respective dates of exit. The exit rate is reviewed at least every three months and, if necessary, it is adjusted to reflect the investment results for the financial year to date.

The initial exit rate, which is set immediately after the computation of the crediting rate for the previous financial year, is the market yield on 10-year Commonwealth bonds applying at the end of the previous financial year, less an adjustment to allow for tax.

For members exiting the MSBS after 1 July 1994, the Trustees determined the following exit rates:

- 8.2% effective from 1 July 1994;
- 7.2% effective from 21 September 1994;
- 4.0% effective from 23 November 1994;
- 1.7% effective from 22 February 1995; and
- 2.5% effective from 1 May 1995.

FUND MANAGERS

The current fund managers are Commonwealth Funds Management (CFM), Bankers Trust (BT) and JP Morgan (JPM). In keeping with the Trustees' 1994–95 policy of allocating approximately equal funds to each manager, the distribution was as follows: ►

ASSET ALLOCATION AS AT 30 JUNE 1995

Asset class	CFM	BT	JPM	Total	% of Fund
	\$m	\$m	\$m	\$m	%
Growth assets					
Australian equities	31.4	42.4	25.3	99.1	33.2
International equities	17.8	20.0	19.6	57.4	19.2
Property	13.5	0.0	15.5	29.0	9.7
Subtotal	62.7	62.4	60.4	185.5	62.1
Defensive assets					
Australian fixed interest	28.3	30.7	20.4	79.4	26.5
International fixed interest	3.0	2.1	7.3	12.4	4.1
Liquids	3.8	1.5	10.6	15.9	5.3
Inflation linked bonds	6.1	0.0	0.0	6.1	2.0
Total	103.9	96.7	98.7	299.3	100.0
% of Total	34.7	32.3	33.0	100.0	

Fund growth since 1991 is illustrated on page 6.

The names and addresses of the fund managers are:

CFM Ltd	BT Asset Management Ltd	JP Morgan Investment
12 Moore Street	Australia Square Tower	Management Australia Ltd
Civic ACT 2600	Sydney NSW 2000	333 Collins Street
		Melbourne Victoria 3000

INVESTMENT NEWS

A NEW INVESTMENT ADVISER APPOINTED

On 3 April 1995, IPAC Securities Ltd began its consultancy as MSBS investment adviser, following the expiry of William M Mercer's contract.

The Trustees, in conjunction with IPAC, are currently undertaking a review of the Fund investment policy. They expect the review to be completed in 1996. There are likely to be significant changes to the investment policy and portfolio structure as a result of the review. These will be reported to members once the review is completed through a revised investment policy booklet.

A MASTER CUSTODIAN APPOINTED

The Trustees appointed Westpac Custodian Nominees Ltd as master custodian to report on the administration of the investments of the MSBS from 1 July 1994.

Westpac provides the Trustees with performance measurement and risk analysis, a consolidated monthly report on the Fund management, and accounting and taxation reports.

CHANGED INVESTMENT ARRANGEMENTS

In order to protect against losses, liabilities, actions, claims or demands, arising from the performance of its functions, the Board has taken out professional indemnity insurance with AMP General Insurance Limited.

BOARD ISSUES

For more information on the management and performance of the Fund, or

INSURANCE AND SUPERANNUATION COMMISSION COMPLIANCE CERTIFICATE

In order to receive favourable tax concessions for 1994-95, the Fund must have satisfied the superannuation fund conditions under the *Superannuation Entities (Taxation) Act 1987* (formerly known as the *Occupational Superannuation Standards Act 1987*) up until the date of the election to become a regulated superannuation fund under the *Superannuation Industry (Supervision) Act 1993* (SIS), on the 29 June 1995. In future years, the Fund will have to comply with SIS requirements. The Board has received a compliance certificate from the Insurance and Superannuation Commission for the 1993-94 year of income. They anticipate receiving a compliance certificate for the 1994-95 year of income.

The Board elected under section 19 of the *Superannuation Industry (Supervision) Act 1993* (SIS), for the Fund to become a regulated Fund for the 1994-95 financial year.

for copies of:

- the 1994-95 audited financial statements (including the Auditor-General's report);
- the MSBS investment policy booklet;
- OSSA compliance notices; and /or
- the MSB Trust Deed and Rules

WRITE TO:

Michele Dawson
The Secretary
MSBS Board of Trustees
PO Box 22
Belconnen ACT 2616

Phone: (06) 252 6698 or (06) 252 5268

Fax: (06) 252 6948

INVESTMENT POLICY

The investment strategy for the MSBS is aimed at maximising long-term returns for members while reducing wide fluctuations that occur in investment markets. As part of their review of the investment policy, the Trustees have resolved to target a long-term return of 5% per annum above inflation (after tax and expenses). In deciding on this target, the Trustees balanced the likelihood of having a negative Fund return in any one year against the much increased payments members can expect over the longer term. The Trustees believe that the additional returns that most members can expect from those monies that must be preserved until retirement will easily compensate for an occasional negative result. It is important that members understand and accept that, from

▶ time to time (approximately 1 year in 7 on average), a negative return may still occur under the more aggressive investment strategy. However, the quantum of the members' benefit should be considerably greater than if a more conservative strategy were adopted.

The Trustees consider that the Fund should continue to follow a long-term investment strategy and not be unduly influenced by short-term performance results. The return of the Fund during 1992–1993 (good) and 1993–1994 (poor) shows how quite different messages can be received if results are considered over only one-year periods. Observing the Fund performance over even two and three years gives a much more realistic view.

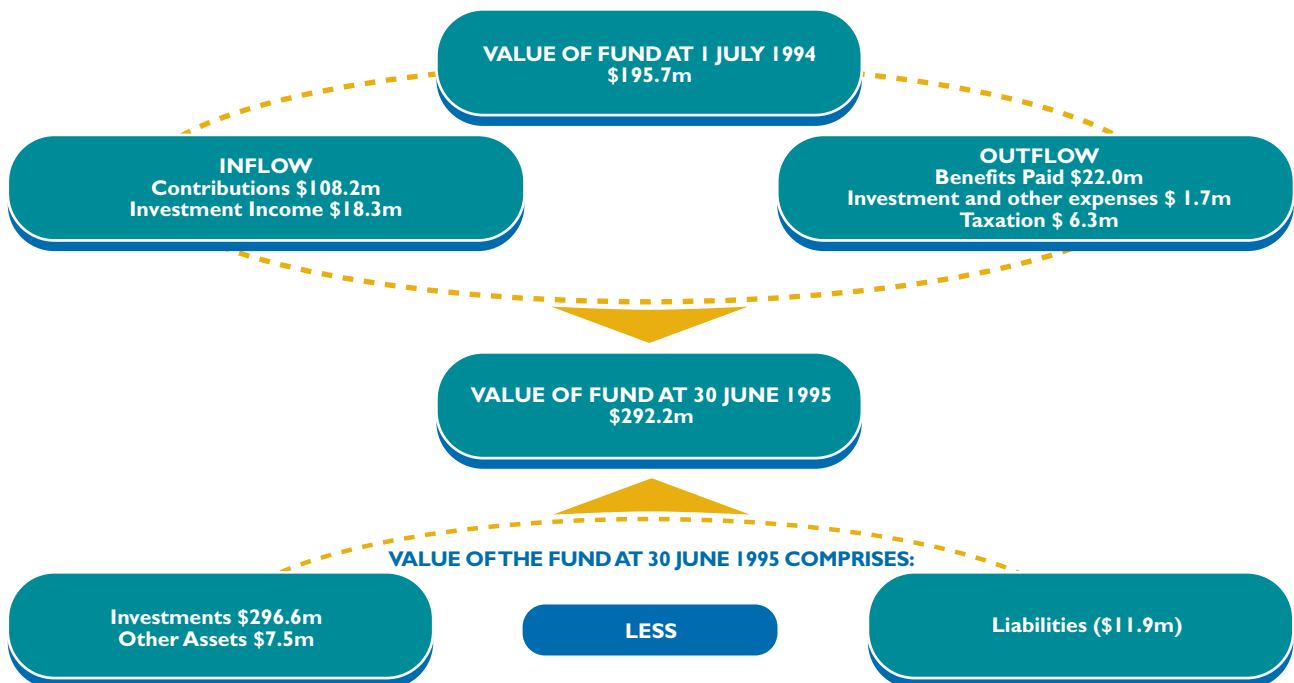
The Trustees are continuing with their policy of broad diversification of investments to lessen the impact of short-term movements, while still securing long-term growth. The three Fund managers carry out the day-to-day investment decisions, and provide a further level of diversification. The Trustees closely monitor these managers and receive independent advice from the investment adviser. The current investment review will assess how further improvements can be made.

INVESTMENT EARNINGS FOR THE LAST THREE YEARS

(after tax, investment fees and other expenses)

1992–93	\$ 8.47 million
1993–94	\$ 6.48 million
1994–95	\$15.53 million

FINANCIAL SUMMARY



Important Notes

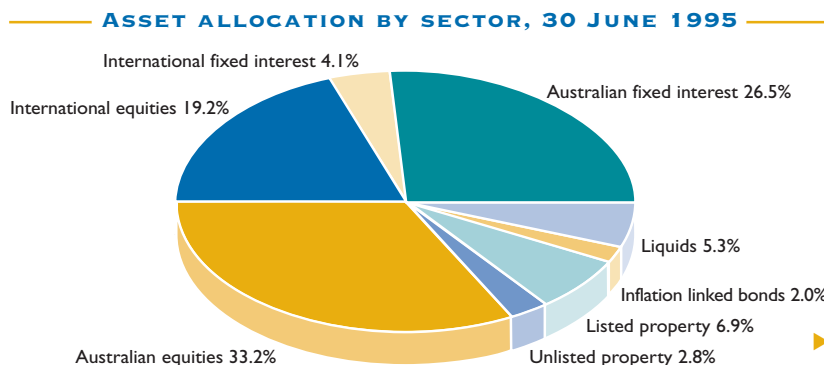
The value of the Fund in the above diagram includes all investment and non-investment assets, and is net of total Fund liabilities

The 1994–95 figures are taken from the annual financial statements currently being prepared by ComSuper in respect of the operations of the Fund. Fully audited financial statements will be included in the Board's 1994–95 annual report to the Parliament, and will be available from ComSuper after the report is tabled in the Parliament.

Copies of the annual report will also be available in your Defence library, or at AGPS bookshops.

ASSET ALLOCATION

Allocating funds between *growth* investments (shares and property) and *defensive* investments (cash and fixed interest) is the most important decision the Trustees make on behalf of members. It has the most impact on the return that can be expected above inflation in the long term (rolling five to seven year periods). The following figure shows the distribution of assets at 30 June 1995.



THE BOARD OF TRUSTEES

The Board consists of five Trustees appointed by the Minister for Defence Science and Personnel under section 21 of the *Military Superannuation and Benefits Act 1991*. Two of the Trustees, nominated by the Minister, must have experience in, and knowledge of, the formulation of government policy and public administration. Two must be members of the Defence Force, nominated by the Chief of the Defence Force, one an Officer and the other a member other than an Officer.

The fifth Trustee, who is also the Chairperson of the Board, is appointed by the Minister after consultation with the Minister for Finance. The Chairperson and the Trustees nominated by the Chief of the Defence Force are appointed for a period not exceeding three years (but are eligible for reappointment), whereas the remaining two Trustees hold office at the Minister's pleasure. Members holding office at 30 June 1995 were:

Sir William Cole (Chairperson) — appointed 18 September 1991; reappointed 23 September 1994. On leave of absence from 25 April 1995 to 8 June 1995 and was reappointed on 9 June 1995.

Formerly Australian Statistician; Secretary, Department of Finance; Chairman, Public Service Board; Secretary, Department of Defence. Sir William chaired the Defence Force Retirement and Death Benefits Scheme Review Committee.

Mr Ian Castles was appointed acting Chairperson from 25 April 1995 to 8 June 1995 while Sir William Cole was on leave of absence.

Air Vice-Marshal Frank Cox AO — appointed 9 March 1995.

Assistant Chief of the Defence Force (Personnel).

Mr Patrick Gourley — appointed 9 August 1993.

First Assistant Secretary, Human Resources and Management Division, Department of Defence.

Mr Kenneth Searson — appointed 27 April 1992.

Commissioner for Superannuation and Chief Executive Officer of ComSuper; Chairman, Defence Force Retirement and Death Benefits Authority; a member of the CSS Board and PSS Board; Federal Councillor of the Association of Superannuation Funds of Australia.

Warrant Officer David Sutherland RAN — appointed 18 September 1991; reappointed 23 September 1994.

Officer In Charge, Fleet Air Arm and Submarine Arm, Career Management Cell, Harman Navy Office.

► During the 1994–95 financial year, the Fund reduced its cash holdings to increase its growth assets by 4% and fixed interest holdings by 3%. The main increases were to Australian and international shares and Australian bonds. These changes improved the Fund's return during the first six months of 1995. The Board's target is to increase the fund's allocation to growth assets to approximately 75%, in order to give members better long-term returns.

BE SUPER-INFORMED

In December 1994, ComSuper sent you (via your pay offices) a new edition of leaflets covering the following topics:

- *Resignation and Retirement Benefits*
- *Provisions for LWOP*
- *Dependants' Benefits*
- *Invalidity Benefits*
- *Maximum Benefit Limit*
- *The Productivity Benefit*
- *Preservation of Benefits*
- *Taxation of Benefits*
- *Rejoining the ADF*

In December 1994, ComSuper also distributed to your pay offices a kit containing the latest *MSBS News Update*, the *Investment Policy* booklet and *The MSBS Book*.

The MSBS Book is a new publication which gives an overview of the MSBS—how it is administered; how your contributions are paid into an investment fund; how the Fund is managed; how its earnings are allocated to you each year; the different types of benefits available and how they are calculated and paid.

NEED MORE INFORMATION?

Superannuation is a very important part of your employment package. Your MSBS benefit will have a great bearing on the kind of lifestyle that you will be able to afford in retirement—so the more you know about your super, the better equipped you will be to make important decisions about superannuation and its effect on your future.

The Trustees are obliged to ensure that you have full access to information about your contributions, your prospective benefits, the management of Fund investments, and anything else that affects your super entitlements.

YOUR EMPLOYER CONTRIBUTES TO YOUR FUTURE

Sgt Moon resigns at age 44 after serving for 25 years and 182 days. Her FAS is \$35 665. Her benefit consists of a lump sum of her member contributions and interest and an employer-financed benefit, which is worked out as follows:

7 years @ 18% = 1.26 x FAS
 13 years @ 23% = 2.99 x FAS
 5 years 182 days @ 28%
 = 1.54 x FAS

Total = 5.79 x FAS
 = 5.79 x \$35 665
 = \$206 500

She can take her member contributions and interest when she finishes work but the employer-financed benefit must be left in the Fund until she retires from the civilian workforce at or after age 55.

There are two parts to the preserved employer-financed benefit. The first part is the 3% productivity component (\$16 250). This amount earns interest at the Fund's crediting rate. The balance (\$190 250), is indexed to the CPI each year.

When Sgt Moon finally retires from the workforce at or after age 55, she can take her accumulated employer-financed benefit as a lump sum, an indexed pension, or a combination of both.

Your employer-financed benefit has two parts:

- the 3% productivity contributions paid into the Fund by the Department of Defence, plus interest; and
- the balance of your employer-financed entitlement paid by the Commonwealth when the benefit becomes payable.

PHASE-IN OF EMPLOYER-FINANCED BENEFIT

If you resign before completing seven years of service, you are entitled to the full amount of your 3% productivity benefit. However, access to the balance of your employer-financed entitlement is phased in over your first seven years of service, as follows:

Completed years of service	% of benefit payable
less than 5	40
5	50
6	75
7	100

HOW IS YOUR BENEFIT CALCULATED?

The amount of your employer-financed benefit depends on your length of service and your final average salary (FAS)—that is, your average salary over the last three years of your service in the Defence Force. The following table shows how your FAS is calculated according to your years of service.

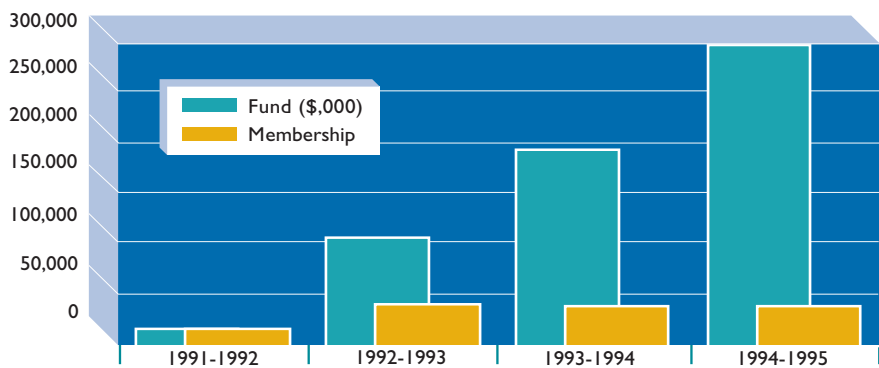
Years of service	% of FAS per year
Enlistment to 7 years	18
7 years 1 day to 20 years	23
20 years 1 day onwards	28

The employer-financed benefit is worked out according to the number of completed years and days of service, as shown in the example on this page.

SCHEME MEMBERSHIP

At 30 June 1995, there were 36 574 contributors to the MSBS—30 113 male and 6461 female. There were 6763 new members and 5533 exits, resulting in an increase in membership of 3.5%.

FUND AND MEMBERSHIP GROWTH, 1991-92 TO 1994-95



Although there was an increase of only 1230 in membership in 1994-95, the size of the Fund (after tax and fees) grew from \$195.7m at 30 June 1994 to \$292.2m at 30 June 1995.

AUDITOR-GENERAL'S REPORT

The Auditor-General carries out an annual audit of the financial statements of the MSBS. In his report for 1993-94, the Auditor-General certified the financial statements without qualification.

The Auditor-General's report is included in the Trustees' annual report to Parliament, which was tabled on 19 October 1994.

THE 1993–94 CREDITING RATE

BACKGROUND

The 1993–94 crediting rate was calculated on the basis of preliminary data available during July 1994, so that it could be included in the member information statements, which were to be distributed in August. The Trustees decided that, if the rate calculated in July was higher or lower than that indicated when the audited financial statements were available, a small adjustment would have to be made to the crediting rate of the following year.

The crediting rate set during July 1994 was 5.4% per annum, while the crediting rate calculated in September from the information contained in the 1993–94 financial statements was 4.4% per annum. The difference must be taken up in the calculation of the 1994–95 crediting rate.

REASONS FOR THE OVERCREDITING

There were two reasons for the overcrediting. The first related to the investment performance of the Fund. The investment managers were asked, in the last week of June, to estimate the performance of their portfolios for the month of June 1994, although Fund performance figures were not available until July. This resulted in an overestimation of performance in June 1994, contributing 0.4% to the 1.0% overstatement in the 1993–94 crediting rate.

Secondly, at the time of calculating the 1993–94 crediting rate, no information was available regarding unpaid benefits as at 30 June 1994—that is, benefits due to members, who exited prior to 30 June 1994, but whose benefits had not yet either been received or processed by ComSuper. In determining the 1993–94 crediting rate, the Trustees therefore estimated a similar number of unpaid benefits at 30 June 1994 as had been outstanding at 30 June 1993. The financial statements showed an increase of \$950,000 in the amount of unpaid benefits as at 30 June 1994 compared with 30 June 1993. This had the effect of reducing the MSB Fund balance as at 30 June 1994, contributing 0.6% to the 1.0% overstatement in the 1993–94 crediting rate.

ACTION TAKEN

As soon as the amount of the overstatement was determined, the Trustees adjusted the exit rate. The exit rate was lowered from 8.2% per annum to 7.2% per annum with effect from 21 September 1994. All exit rates declared since that time (*see* page 2) have been similarly adjusted.

The Trustees did not expect that the difference in the crediting rate calculated in July 1994 and the crediting rate calculated following audit of the financial statements would be as great as 1.0%, and have consequently given considerable thought to the process of calculating the crediting rate in the future.

The Trustees decided not to determine the 1994–95 crediting rate until ComSuper had received the investment accounting reports for 1994–95, from which the Fund performance for the financial year could be ascertained. This avoided the estimating process which contributed to the overstatement of the 1993–94 crediting rate.

Further, most of the benefits outstanding at 30 June 1995 would have been processed, thus providing more reliable information for the unpaid benefits at 30 June 1995.

This would have the effect of delaying the member information statements by several weeks or more, but the Trustees considered that this would be preferable to an inaccurate estimate being made.

EFFECT OF 1994–95 CREDITING RATE

The crediting rate for the financial year 1994–95 is 5.8%. The crediting rate is lower than it might otherwise have been because of the over-crediting in 1993–94.

SUPERANNUATION

PRESERVATION

CHANGES

In 1992, the Treasurer released the Government's 'Security in Retirement' package, which contained a number of planned simplifications and enhancements to existing retirement income policies and rules.

There were two proposals that affect MSBS members:

- the preservation of part of the member benefit from 1 July 1996; and
- the extended age for preservation from 55 to 60 for those born after 1960.

PRESERVATION OF THE MEMBER BENEFIT

From 1 July 1996, the portion of MSBS benefit a member will be able to access as a lump sum before genuine retirement from the workforce will be limited to the greater of:

- the member's contributions to the Fund (without interest); or
- the amount that would have been paid to the member if he or she had resigned on 1 July 1996, indexed according to the change in average weekly ordinary time earnings (AWOTE).

Retirement means either:

- you cease employment at or after age 60; or
- you cease employment between the ages of 55 and 60 and intend never to work again for more than 10 hours a week.

The portion of the member benefit that cannot be accessed must be preserved in the Fund, where it will continue to earn interest, until the member reaches preservation age.

► **EXTENSION OF THE PRESERVATION AGE**

The Government has announced its intention to introduce legislation regarding the extension of the ages for claiming preserved benefits.

The current preservation age is 55. This means that all superannuation benefits which must be preserved under SIS cannot be accessed before the age of 55.

The Government has proposed that the preservation age be extended from 55 to 60 on a phased-in scale, and that only persons born after 1960 will be affected, as shown in the following table.

Person Born	Preservation age
before July 1960	55
July 1960 to June 1961	56
July 1961 to June 1962	57
July 1962 to June 1963	58
July 1963 to June 1964	59
after June 1964	60

This means that the change to age 60 will not be in place until the year 2025.

Members retiring before they reach their preservation age will be allowed access to a partial lump-sum benefit, *provided they take the remainder of their benefit as a non-commutable lifetime pension*. The extent of the lump sum depends on age at retirement, as shown in the following table.

Age Born	Limit of lump sum (\$)*
55	30 000
56	40 000
57	50 000
58	60 000
59	76 949

*Dollars are quoted in 1 July 1992 values. These values will be adjusted to changes in (AWOTE).

LEGISLATIVE CHANGES

Since the last newsletter, the following amendments were made to the MSB Act and Rules.

INSTRUMENT NUMBER 1 OF 1994

This instrument amends Rule 7 to include members who have been granted leave without pay for compassionate reasons. A member granted leave without pay on compassionate grounds may seek the Trustees' approval to contribute for a maximum of two years during the leave, providing the leave without pay does not exceed four years.

In this circumstance, contributions will increase the amount of member benefit, but no employer-financed benefit will accrue.

Although the period of leave will not count towards *qualifying service* for the retention benefit, *continuity of service* for the retention benefit will not be broken, provided the member contributes to the Scheme for the full period of leave or for the maximum contributory period if the leave exceeds two years.

If a member does not contribute, the 15-year qualifying period for the retention benefit will recommence from the time the member returns to work.

INSTRUMENT NUMBER 2 OF 1994

This instrument amends Rules 51 and 52 which in effect allow the partial release of a preserved employer-financed benefit, subject to ISC recommendation. The amendment to Rule 52 also necessitated the introduction of Schedule 4A to cover the calculation of a notional employer-financed benefit.

INSTRUMENT NUMBER 3 OF 1994

This instrument amends Schedule 10 (Transfer Value) which allows members, who had a previous service debt under the DFRDB Scheme at the time of transfer to MSBS, a further period in which to pay off that debt as a lump sum, rather than have it offset against the transfer value. This arrangement applied only to those members who were not previously advised of their rights to pay off the debt as a lump sum in the required time.

THE MSB ACT

The MSB Act was amended to ensure that the MSBS complies with the *Superannuation Industry (Supervision) Act 1993* (SIS).

The Defence Legislation Amendment Act 1995

This Act received royal assent on 15 June 1995.

INSTRUMENT NO. 1 OF 1995

The MSB Trust Deed and Rules were amended so that they comply with the SIS Act. All references to the *Occupational Superannuation Standards Act 1987* (OSSA) have been replaced with references to the SIS Regulations.

Instrument No. 1 of 1995 also amended Schedule 8 of the MSB Rules to ensure that MSB employer contribution percentages were in line with the Superannuation Guarantee Charge (SGC) requirements effective on 1 July 1995.

