

**AUSTRALIAN PRUDENTIAL REGULATION  
AUTHORITY**

**SUPERANNUATION CIRCULAR NO III.A.6**

**WINDING-UP A SUPERANNUATION FUND**

*April 2002*

### **DISCLAIMER AND COPYRIGHT NOTICE**

1. The purpose of this Circular is to provide general guidance on issues arising out of the legislation under which the Australian Prudential Regulation Authority ("APRA") regulates particular superannuation entities. It is not exhaustive in its coverage of rights or obligations under any law.
2. This Circular is based on APRA's interpretation of the relevant legislation in respect of the superannuation entities for which it is the regulator and has no legal status or legal effect whatsoever. Any reference to self managed superannuation funds is for general assistance only. Trustees of self managed funds should seek appropriate guidance from the Australian Taxation Office in respect of the application of the legislation in respect of those funds.
3. This Circular may be affected by changes to legislation. APRA accepts no responsibility for the accuracy, completeness or currency of the material included in this Circular.
4. Users of this Circular are encouraged to obtain professional advice on the relevant legislation and to exercise their own skill and care in relation to any material contained in this Circular.
5. APRA disclaims any and all liability or responsibility for any loss or damages arising out of any use of, or reliance on, this Circular.
6. This Circular is copyright. You may use and reproduce this material in an unaltered form only for your personal non-commercial use or non-commercial use within your organisation. Apart from any use permitted under the *Copyright Act 1968*, all other rights are reserved. Requests for other types of use should be directed to APRA.

<b>Contents</b>	<b>Paragraph</b>
<b>Objective</b>	1
<b>Introduction</b>	2
<b>Comment</b>	7
Summary of Legislative Requirements	7
<b>Primary Issues</b>	8
Timing issues	10
Lodgement of the wind-up return	14
<b>Other matters</b>	15
Obligations of Actuaries and Auditors	15
Specific risks for public offer funds	16
Large funds falling below the 5 member threshold	17
<b>Guidance in relation to wind-ups</b>	19

## Objective

1. The aim of this Circular is to set out APRA's views as to the requirements of the *Superannuation Industry Supervision Act 1993* (SIS) for winding up a superannuation fund. This circular is not aimed at self managed superannuation funds. Trustees of such funds should seek appropriate guidance from the Australian Taxation Office.

## Introduction

2. The terms "wind-up", "termination" or "closure" are used interchangeably in relation to superannuation funds. In general, a superannuation fund may be wound up for one or more of the following reasons:

- as a consequence of the wind-up or liquidation of the principal employer;
- a takeover/amalgamation of the employer sponsor where superannuation is also subject to a consolidation process;
- insolvency of the fund;
- the result of rationalisation into a single arrangement of various existing superannuation arrangements that cover a number of different groups of employees; or
- a decision by the employer sponsor to replace its existing superannuation arrangements for employees with a new arrangement.

3. Where a wind-up occurs as a result of transferring benefits to another scheme, the "Successor Fund provisions" of SIS may be relevant. Circular I.C.4 - Equivalent Rights for Members in Successor Fund Transfers, issued by APRA in February 2001, should also be consulted in all such cases (eg. where an employer withdraws support from a defined benefit plan and commences to pay employee contributions into an accumulation plan).

## Comment

### Summary of Legislative Requirements

4. The SIS legislation imposes a number of requirements on trustees once a decision has been made to wind up a superannuation fund. The following non exhaustive list may be useful in highlighting some of the requirements specifically relevant to wind-ups:

- **SIS Act Section 36** – requires the trustee of a superannuation fund to lodge a specific annual return with APRA.
- **SIS Act Section 106(1)** – requires APRA be notified of a significant adverse event affecting the financial position of the fund.
- **SIS Act Section 117** - outlines the circumstances in which amounts of surplus may be paid out of an employer-sponsored fund to a standard employer sponsor.

It should be noted that ownership of a surplus is not always clear (in terms of the fund's governing rules). There has been a history of litigation concerning the return of surplus to an employer where ownership is unclear. As this involves additional risk, APRA would generally expect a trustee to seek legal advice in such circumstances.

- **SIS Act Section 121A** – prohibits a person from being a trustee of a fund with fewer than 5 members (other than a self-managed superannuation fund) unless the person is an approved trustee.
- **SIS Act Section 129** - places certain reporting obligations on Actuaries and Auditors.
- **SIS Regulation 1.03(1)** - defines a “successor fund” (refer also to Circular I.C.4 – Equivalent Rights for Members in Successor Fund Transfers).
- **SIS Regulation 4.05(2)(b)** - allows trustees to add a relevant enabling clause in order to proceed with a wind-up (where the governing rules do not permit the wind-up of the fund).
- **SIS Regulation 6.29** - allows a transfer of member benefits with member consent; or allows a transfer to a successor fund.
- **SIS Regulations (Division 9.4)** – relates to winding-up of defined benefit funds.
- **SIS Regulations 9.19(4), 9.25(5), 9.39(4), 9.45(5)** - governs the payment and value of benefits.
- **SIS Regulation 11.07(3)&(4)** – requires written notice to APRA (as soon as practicable, and in any event prior to the commencement of the winding-up) of a trustee's decision to wind up a fund.
- **SIS Regulation 13.16** – concerns any reduction in members' accrued benefits.
- **Public Offer Funds** – The Trustees of these funds may also under certain obligations in respect of reporting significant changes, etc to APRA under the Instrument of Approval.

## Primary issues

5. APRA's primary concern is the equitable distribution of assets and treatment of member benefits. Key objectives of any wind-up plan should be to ensure that:

- members are informed of the in-principle decision to terminate the fund and they are provided with details of future arrangements / options in a clear, effective and timely manner. Notification should take place before the winding-up commences; and
- the wind-up process is carried out smoothly, without delays or detriment to the members' accrued benefits and in accordance with SIS and the governing rules.

6. It must be remembered that any interpretation of benefits and the right of a member to those benefits must be considered in the context of the governing rules of the fund as well as legislative requirements. The governing rules of the fund may

prescribe, in general terms, the circumstances in which a fund could be terminated. However, it is unlikely that they would outline all specific steps required to complete the wind-up. In the case of some public offer funds the governing rules may outline a more detailed process that may include a resolution passed by the majority of members and endorsed by the trustee board.

7. Examples of external events that may impact on funds (under the governing rules) include:

- an employer-sponsor giving notice to the trustee of a defined benefit fund that they are terminating contributions to the fund; and
- an employer's participation in the fund terminating in other circumstances (for example, an associated employer leaving a corporate superannuation fund or a participating employer leaving a Master Trust arrangement).

8. In such situations, the governing rules frequently state that certain benefits would cease (such as insured benefits) at the time that contributions/participation cease. In some circumstances the governing rules may require that the fund be wound up. Generally, APRA would expect a trustee of the original fund to seek legal advice in such circumstances.

9. By way of illustration of the principle of an external event referred to above, the following example is provided:

- an employer sponsor currently makes contributions on behalf of its employees into an employer sponsored fund (original fund). In the example, the employer wishes to cease contributions into the original fund and commence contributions into a Master Trust (new fund). The employer also wishes that the existing balances be transferred from the original fund to the new fund.
- under the governing rules of the original fund in this example, on cessation of contributions by an employer sponsor, those employees are no longer eligible to be members of the fund. As such their benefits must be transferred out of the fund to another fund or to an eligible rollover fund (ERF). Once again, Circular I.C.4 - Equivalent Rights for Members in Successor Fund Transfers is relevant.

### **Timing issues**

10. To avoid delays in winding up a fund, trustees may enter into a deed of arrangement so that the date of transfer of legal title to assets occurs on an agreed date regardless of when the physical transfer of assets occurs. The effective date of wind-up should then be the transfer date stipulated in the deed.

11. Where the trustee has not entered into a deed of arrangement, the effective date of wind-up is when the assets (and associated liabilities and member entitlements) have been physically transferred. This may be a long drawn out process if proper planning is not undertaken (further guidance on this issue is available at the end of this circular). This may result in further financial statements and returns having to be issued before the final set of wind-up financial statements and returns can be prepared.

12. Funds should wait until they have no assets and liabilities before lodging a wind-up return. A prudent trustee may "over retain" assets in the fund to meet minor residual liabilities (eg taxes, legal fees, outstanding APRA levies etc). This will most

likely mean that there will be additional funds to be distributed to members (and therefore that a final member distribution will be one of the last functions). The wind-up return would generally be lodged at this point.

13. However, it is possible that (despite the best efforts of the trustee) a fund may receive unexpected moneys (eg. an unexpected tax refund) after member benefits have been transferred out of the fund and the wind-up return lodged. As stated, APRA's primary interest is the equitable distribution of assets and treatment of member benefits. Therefore, if unexpected moneys are subsequently received in respect of the fund, they may be distributed. Of course, members retain an equitable right to any such moneys. APRA should be informed and approval granted where there are no members to approve distribution.

### **Lodgement of the wind-up return**

14. A specific wind-up return must be lodged with APRA as soon as possible after the wind-up is completed (it is not sufficient to indicate on an annual return that a wind-up has taken place). Following changes on 1 July 1998 to levy arrangements there is no levy payable on lodgement of a wind-up return. If a fund is not wound-up at the end of the year of income, an annual return will need to be lodged at the normal time under Section 36 of SIS (which will trigger a levy for that year). A wind-up return will still be required to finalise the wind-up process. Similarly, a superannuation fund is not automatically relieved of its obligation to hold an actuarial review by winding up. Trustees may request relief from this requirement upon notifying APRA of the decision to wind up the fund.

## **Other matters**

### **Obligations of Actuaries and Auditors**

#### ***Section 129***

15. Section 129 places certain reporting obligations on actuaries and auditors. The question has arisen as to whether an auditor needs to comply with s129 especially where the audit is being undertaken after the completion of the transfer of members and assets. It is APRA's view that s129 applies until the fund is properly wound up. In fact, given that there could be additional opportunities for fraud or non-compliance in the confusion of the wind-up, APRA strongly stresses the importance of these s129 obligations.

### **Specific risks for public offer funds**

16. Factors for the trustee to consider include the potential for concern among members (which could lead to an increase in requests for redemption unless they receive full information); adverse publicity and/or implications for associated entities (where the public offer fund is part of a financial industry group).

## **Large funds falling below the 5 member threshold**

### ***Section 121A***

17. It has been recognised that, in circumstances where a larger employer-sponsored fund is being wound up, at some point the number of remaining members may reduce to the point that the fund would inadvertently be affected by the trustee requirements for funds with fewer than 5 members.

18. Pending amendment to s.121A<sup>1</sup>, APRA will not take action against a trustee solely on the basis that it inadvertently breached the trustee requirements relating to funds with fewer than 5 members during the wind-up process (provided the wind-up is progressed in a timely fashion). For example, if a corporate fund with 50 members winds down within a period, even though it falls below 5 members it would still be classified as a corporate fund for the whole of the period or until the date of wind-up. If the fund crosses a reporting period (ie. starts a reporting period with less than 5 members) and is still in the process of winding-up, APRA would maintain its "corporate" fund status.

## **Guidance in relation to wind-ups**

### ***Section 106(1), 117, Regulation 9.19(4); 9.25(5); 9.39(4); 9.45(5), 11.07(3) and (4), 13.16***

19. The following guidance could be used as an approximate wind-up time-line. It is not definitive, as each fund will have different characteristics (eg. some funds may be required to follow a process laid out in the governing rules). However, it sets out a general process whereby the trustee makes appropriate provisions, makes all possible payments and lodges a wind-up return.

20. Trustees should take appropriate care to support any decisions made in connection with the wind-up process (to reduce the level of risk inherent in the process). For example, equal representation should be maintained during the decision making process.

21. Having regard to the objectives of a wind-up, trustees should prepare an action plan outlining all steps necessary for its completion (APRA would not expect wind-ups to take longer than 6-12 months). It may be necessary for a trustee to seek independent advice concerning the wind-up process. While SIS does not specifically set out the steps to be followed to complete a wind-up, the following matters should be included (where relevant).

### **Advising APRA**

22. APRA should be informed of the decision to wind up the fund as soon as practicable, and in accordance with SIS Regulation 11.07(3) and (4). In general, a fund should initially advise their APRA Relationship Manager (or the Relationship Manager of their Approved Trustee) of the intention to wind up, and provide details of

---

<sup>1</sup> The proposed amendment is contained in Financial Sector Legislation Amendment Bill (No.1) 2002



the planned process and anticipated timing (and particularly when the wind-up return is to be lodged).

### **Planning**

23. This circular does not attempt to cover all possible wind-up planning issues, as it is likely that these will differ on a fund by fund basis. For example, there may be questions concerning the ownership of documentation. It may also be necessary for trustees to establish a new registered office and files may need to be moved or stored.

24. A fund “disaster recovery plan” may need to be activated in the event of a wind-up. The plan could cover factors such as the recovery of any unpaid employer contributions or possible avenues to conduct business (where existing premises are no longer available).

25. Planning should also cover the basis of the fund’s wind-up (eg. “successor” fund provisions; or nomination of one or more funds to which benefits may be transferred upon consent by members, or allowing members to select the fund of their choice). Consideration should be given as to whether there was any event in the years preceding the wind-up which may have led any member / group of members to be materially advantaged or disadvantaged by the timing of their departure from the fund.

### **Risk evaluation**

26. It is important to note any additional risks that a fund (particularly a smaller corporate fund) may be subject to in the event of a wind-up. For example, the risk of fraud may be higher during a wind-up (eg. member discrepancies may be identified or there may be a failure to confirm receipt of transferred benefits). The right of fund members to any fund surplus or “windfall gain” should also be carefully calculated.

### **Record keeping**

27. The trustee minutes should record the decision to wind up the fund together with the trustees’ action plan and a complete timetable.

### **Informing members**

28. Members should be informed of the wind-up decision, the reasons for the change, possible changes to the benefit structure and future superannuation arrangements / options, including continuity or otherwise of existing insurance cover and/or contact details for claims made after cessation in respect of events that occurred prior to wind-up.

### **Accounting and audit issues**

29. The production and audit of the final set of the financial statements should be arranged. The notes to and forming part of the financial reports of the terminating fund should disclose any “receiving fund”, together with the total value of the assets and liabilities transferred by the terminating fund. Any outstanding concerns from the previous year’s audit should be resolved and any concerns with the current process determined. A particular focus should be placed on assessing fund assets and the distribution of those assets.

30. Appropriate provisions should be made for various outstanding expenses (eg. taxation provision, insurance premiums and administration charges). Special care should be taken with the calculation of the taxation expense for the final accounting/tax period of the fund. Given the complexities surrounding these issues, this is an area of significant risk (eg. the calculation of capital gains tax and qualification for taxation concessions where there has been a change in the trustee, but no change in the beneficial interest of the trust).

31. All investment returns should be taken into account in the determination of the crediting rate to members' accounts. Orderly realisation of assets may be of concern for certain (smaller) funds, since certain assets (such as property) may not be readily realisable (requiring increased lead-time in the wind-up process). Where assets are transferred in-specie to a successor fund, care should be taken with the valuation of such assets (eg. establishing arms length market value). The date of valuing assets, which are transferred in specie, should be consistent with or approximate the effective date of transfer of legal title of the assets.

32. A reconciliation of member balances to the net assets of the fund should be undertaken. The external auditor should obtain an understanding of the methodology applied in calculating member balances on wind-up and the application of the benefit calculation methodology should be tested on a sample basis.

### **Asset management**

33. A decision should be made on the distribution of any surplus either to members, standard employer sponsor or both. In the case of returning a surplus to an employer sponsor, trustees must comply with Section 117 of SIS. This includes a requirement to provide members with three months notice of the intention to return a surplus to the employer sponsor, and for the decision to be made in compliance with equal representation requirements. This latter requirement may be an issue if the fund membership is declining rapidly. Member protection should be applied to any small balances held in the fund during the wind-up process.

34. Where a fund is technically insolvent (either through actuarial assessment or where minimum benefits exceed the net realisable value of fund assets), all SIS rules (governing the payment and value of benefits) must be adhered to (eg. SIS Regulations 9.19(4), 9.25(5), 9.39(4), 9.45(5)). This would be considered a significant adverse event requiring APRA be notified accordingly (there is also a requirement to notify members). Any reduction in members' accrued benefits must be in accordance with the provisions of SIS Regulation 13.16. (Regulation 13.16 applies to changes made to the governing rules and to actions by the trustee, not to reduction due to poor investment performance).

### **Successor Fund issues**

35. If the "successor" fund option is adopted, members should be provided with a Handbook / Member Booklet outlining the details of benefits/contributions and the manner of operation of the new fund. Trustees must be satisfied that the successor fund provisions apply, by determining whether the chosen transferee fund confers "equivalent rights" with respect to members' benefits, when compared with the transferor fund (refer to Circular I.C.4 - Equivalent Rights for Members in Successor Fund Transfers).

36. Members should be provided with an explanation of the conditions of transfer and, where appropriate, given comparisons of the benefits under the existing and the new arrangements. Advice should be given on how to complete the required forms (eg. transfer / consent, application, insurance, nomination of beneficiary, and tax file notification).

### **Regulatory and other issues**

37. The transfer of benefits into the new superannuation fund(s) should be arranged and relevant confirmations (from those superannuation funds) obtained. The payment of all outstanding expenses should be organised.

38. The APRA wind-up return should be completed and lodged. In addition there may be other requirements that must be satisfied in relation to other bodies (eg. ASIC or the ATO. For example, fund trustees must ensure that any outstanding taxation obligations are met (eg. completion and lodgement of an income tax return and reporting of surcharge and RBL information to the ATO). This will help to ensure that there are no other items (that the ATO administers) that remain outstanding and which could impact on the winding-up of the fund.