THE PROPOSED NEW MILITARY SUPERANNUATION SCHEME

THE DFWA POSITION - February 2015

Current Situation

Full time ADF members must be members of one of two military superannuation schemes:

1. **Defence Force Retirement and Death Benefits (DFRDB) Scheme.** DFRDB opened on 1 October 1972 and closed to new members on 1 October 1991. 2,733 serving ADF members still contribute to DFRDB. DFRDB contributors must pay 5.5% of their salary to their employer, the government. They paid approximately $17 million to the government in 2013-14.
2. **Military Superannuation and Benefits Scheme (MSBS).** MSBS is commonly known as *Military Super*. All full time ADF members who joined after 1 October 1991 must be MSBS members. 56,470 serving ADF members contribute to MSBS. MSBS members must pay a minimum of 5.0% of their salary to the government's Commonwealth Superannuation Corporation. They paid approximately $250 million to the government in 2013-14.

Part time (Reserve) ADF members are normally not permitted to join any military superannuation scheme unless on continuous full time service.

An earlier military superannuation scheme, the Defence Force Retirement Benefits (DFRB) scheme closed on 30 September 1972. All serving DFRB members were then compulsorily transferred to DFRDB (and their accumulated funds transferred to government coffers). DFRB should not be confused with DFRDB.

DFRDB is a *defined benefits* scheme. Modern civilian schemes are *accumulation* schemes, sometimes called *defined contributions* schemes. MSBS is a "hybrid" scheme because it is partly *defined benefits* and partly *accumulation*.

What's Proposed

The government in 2014 announced that a new superannuation arrangement for ADF members, known as *ADF Super*, will commence from 1 July 2016.

The government says that *ADF Super* will have these features:

- Individual choice over which superannuation scheme they belong to. Individuals may join *ADF Super* or a commercial scheme.
- Ability to transfer members' accumulated benefits to another fund if they leave the ADF before preservation age.
- No requirement for any member contribution to *ADF Super*.
- An employer contribution rate of 15.4 per cent, increasing to 18 per cent during periods of war-like service. The Government says this would be "in recognition of the unique nature of military service". *(Editor's Note: this term can be traced to your Association's push in recent years for government and the community to recognise the unique nature of military service. The term is now in widespread use. The unique nature of military service is discussed elsewhere in this edition of "Camaraderie".)*
- Death and invalidity cover under the new arrangements will be at least equivalent to current MSBS benefits. This will be covered under separate legislation and will be known as *ADF Cover*.

The new *ADF Super* scheme will apply to:

1. those joining the ADF from 1 July 2016, and
2. serving and returning members of the Military Superannuation and Benefits Scheme (MSBS) who choose to join the new scheme.

MSBS will be closed to new members from 1 July 2016. There will be no compulsion for current or returning MSBS members to join *ADF Super*. But, importantly, the government says that MSBS members who choose to join *ADF Super* will not be permitted to transfer the 'employer' component of their MSBS benefit to the new scheme which means the bulk of their entitlement will remain "preserved" under the present arrangements.

Defence Force Retirement and Death Benefits (DFRDB) scheme contributing members will not be permitted to join *ADF Super*.

ADF Super will be the default fund for ADF members who do not nominate an alternative scheme. It will be established and managed by the Commonwealth Superannuation Corporation (CSC). CSC currently administers all other Commonwealth schemes, including all current and former military superannuation schemes.

The proposed new scheme has no impact on the recent (1 July 2014) fair indexation of certain DFRB and DFRDB military superannuation pensions.

The DFWA View

DFWA does not endorse any waste of taxpayer money in either the short or the longer term, including waste associated with public sector (military, parliamentary, public service) superannuation. But unique penalties applying only to military service are unacceptable to us – and should be equally unacceptable to the government and to the Australian taxpayer.

DFWA has no objection *in principle* to an ADF accumulation scheme with no compulsion on members to contribute. But we have significant reservations about some of the proposed features of the government's *ADF Super* proposal because it does not adequately recognise the unique nature of military service.

A Unique Career

The vast majority of people who enlist in the ADF do not intend to pursue a lifetime Service career. Indeed the ADF can only offer lifetime careers to a small proportion of those who enlist. This is because an effective ADF fighting force demands a large core group of younger adults in its fighting ranks. This core group is constantly renewed by a steady influx of new recruits to keep the core group 'young'. Turnover is high. So it should be.

Common sense says that ADF service is not a long term prospect for most ADF members. If it were otherwise we would see platoons of 60 year old infantrymen hobbling around Afghanistan.

By way of concrete illustration, only 13.8% of MSBS contributors have more than 20 years ADF service. A thumping 60.7% have less than nine years ADF service. Meanwhile, only 16.3% of public servants who contribute to their PSS superannuation scheme have less than nine years service.

And ADF people are significantly 'younger' than the public service. MSBS contributors boast an average age of well under 29 years whereas the average age of PSS public service contributors is well over 45 years.

The government and its advisors need to recognise that the ADF is not the public service. Military service is unique.

'Employer' Contribution

For the new scheme, the government proposes a standard 'employer' contribution of 15.4%, the same as for the latest public service accumulation scheme (PSSap).

Quite simply, we ask why the *ADF Super* scheme and the public service scheme are to be based on the same government contribution? This essentially puts ADF members and public servants in the same category, i.e. without any acknowledgement of the unique nature of military service.

The government recently responded to our queries by advising that:

1. the government's contribution for ADF personnel will be based on a gross salary 'package', i.e. daily rate of pay, plus service allowance, plus specialist allowances, etc, inferring that that the government's contribution for public servants is calculated simply on base salary, and

2. an extra 2.6% contribution will be made to ADF personnel deployed on operations classified as war like.

The DFWA has fundamental difficulties with the government's response.

On the first point, the proposal to give the ADF and the public service the same 'peacetime' rate of 15.4% is clearly wrong as it appears to be based on the assumption/principle that ADF members are, in the eyes of the government, simply government employees doing the same type of work as public servants when "back home". That suggestion is categorically rejected.

A moment's thought will acknowledge the hazardous nature of ADF peacetime training, which is necessary in order to prepare for war. DFWA dismisses out of hand any notion that ADF training activities in Australia are akin to working in the public service.

This difference was recognised in the 2007 Podger Review into military superannuation. Podger called for a new accumulation scheme, with employer contributions increasing with length of service (to 16%, 23% and 28% of superannuable salary).

Further, we reject any suggestion that Service Allowance is in some way 'danger money' to compensate for death and injury.

On the second point, an increased contribution when on operational service, the difficulties in administering such an arrangement are likely to be significant. And operational (warlike) service is often identified in retrospect, so how will "back pay" be calculated? What if a member has retired, accessed their superannuation, then find some past service is deemed "warlike"? DFWA foresees a bureaucratic nightmare if this proposal goes ahead.

And why select 2.6%? The only rationale we can see is that it will add up to a nice round number.

But, of more significance, all members of the ADF serve for a common purpose. The idea of "us" (those not on operational service) and "them" (those on operational service) goes against the very fundamentals of military service. It also goes against a basic principle underpinning the idea of the unique nature of military service – that military service is unique to *all* serving ADF members, not just those at the sharp end on a given day.

Put another way, while recognising that service is rendered in a variety of circumstances, both on operations and in peacetime duties, all members of the defence force are either *giving* warlike service or are *liable* to give such service at the sole direction of the "employer" (who is making the *ADF Super* contribution). The "employee" has no control over the nature of the service performed or the timeframe within which his or her service will take place.

DFWA therefore believes that the *ADF Super* 'employer' contribution rate must recognise the unique nature of military service and must be consistent regardless of where a contributing member serves at any point of time.

We believe that the contribution rate itself should have a nexus with the Notional Employer Contribution Rates (NECR) that presently apply to MSBS and DFRDB because the NECR for these schemes help recognise, in a tangible way, the unique nature of military service.

The DFWA therefore believes that the proposed employer contribution rate of 15.4% for *ADF Super* (a rate which clearly does not recognise the unique nature of military service) must be increased for all ADF members, regardless of where they are posted. The contribution should be the same for all service, and at least at the level contemplated for warlike service - 18% - based on the member's gross salary. This rate would recognise the higher NECR provided to MSBS and the offsetting fact that *ADF Super* members would not be compelled to contribute out of their own pocket to their own superannuation – as is now the case – meaning that take-home pay would increase.

Alternatively, the Podger recommendations – whereby 'employer' contributions increase with length of service – could be considered for *ADF Super*.

Finally, note that the DFWA does not seek a nexus with the extraordinarily generous NECR applying to the pre-2004 parliamentary superannuation scheme.

Reserve Forces

The government says that *ADF Super* will not extend to part time members of the ADF Reserves. Given that all major political parties in Australia are committed to compulsory universal superannuation for all work performed, part time or full time, the government's position is indefensible.

DFWA strongly supports 'employer' superannuation for service in the ADF Reserves, with no offsetting provisions. Part-time ADF members should not be discriminated against.

MSBS Issues

MSBS contributors serving when the new *ADF Super* scheme comes into force may join the new scheme. They will be able to transfer their personal compulsory MSBS contributions (and earnings accrued) to the new scheme if they wish. However they will not be able to access their employer's contributions to MSBS, either at that time or when they leave the ADF. Instead, their government MSBS contributions will be preserved within MSBS until they retire finally from the workforce, indexed only to the totally inadequate Consumer Price Index (CPI).

The DFWA strongly opposes this arrangement. No other Australian in a modern superannuation scheme is unable to access their employer's contribution in order to transfer to a scheme of their choice.

To add insult to injury, because the employer's contribution is indexed only to CPI, the real value ("purchasing power") of the 'employer' contribution will degrade significantly over the many years until the member reaches retirement age.

Modern Australian superannuation schemes enjoy a return of around 7% per annum over the long term. CPI averages around 3% over the long term. The difference can mean a long term loss of hundreds of thousands of dollars to individual MSBS members, merely because he or she was an ADF member. And there is no benefit to the taxpayer. That's unacceptable.

Also note that the 'employer' contribution to MSBS is strictly notional. It exists on paper but not in the bank. There are no real dollars anywhere, and the payments will be made out of government budgets (or possibly, after 2020, out of the Future Fund).

The only beneficiary of this unacceptable arrangement is the government of the day, because its notional 'employer' contribution will be paid by future generations. It is not a cash cost to today's budget, meaning that today's budget looks good while tomorrow's will be a disaster.

But that's a problem for a future government, so governments since 1972 do not worry about it.

DFWA hastens to add that this looming budget disaster was formally recognised in 2006 when the then government established the Future Fund. The Future Fund was designed to cater for the older military and public service superannuation schemes, which were (and are) unfunded. New schemes such as *ADF Super* should stand on their own financial feet.

But there is no justification for preventing MSBS members from transferring all contributions – their own and their employer's – to the new *ADF Super* or to another superannuation fund.

DFWA strongly opposes the singling-out of ADF men and women for the government's punitive transfer measure. And, importantly, this penalty on ADF men and women does not benefit the taxpayer.

MSBS members should be able to transfer their accumulated government funded MSBS contributions to an *ADF Super* account if they elect to transfer to *ADF Super*, or to another fund of their choosing when they separate from the ADF.

The Future

The proposed *ADF Super* scheme, if properly designed (which, as currently proposed, we believe is not) and implemented, can be a positive development for both the ADF and the taxpayer, by recognising in a tangible way the unique nature of military service.

The DFWA will continue to lobby the government on the matters discussed above and for the changes we propose. We are in regular formal and informal contact with government ministers and the bureaucracy, and will continue to push for changes that will be in the best interests of members of the ADF, their families and ultimately the nation.

It is also important that individuals also lobby their local members by bringing these matters to their attention.

It is anticipated that these matters will be decided by Government by way of legislation to be introduced into the Federal Parliament in mid 2015.

(Commonwealth superannuation scheme data is taken from the 2013-14 Annual Report of the Commonwealth Superannuation Corporation.)