

The Parliament of the Commonwealth of Australia

A ‘Reasonable and Secure’ Retirement?

**The benefit design of Commonwealth public sector and
defence force unfunded superannuation
funds and schemes**

SENATE SELECT COMMITTEE
ON SUPERANNUATION AND FINANCIAL SERVICES
April 2001

Commonwealth of Australia

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PREFACE

This report responds to the expressed concerns of Commonwealth superannuants that the benefit design of Commonwealth public sector and defence force unfunded superannuation schemes is not delivering them a ‘reasonable and secure’ retirement income. Often perceived as a relatively privileged group benefiting from a comparatively generous superannuation arrangement, Commonwealth superannuants were vocal in explaining that the perception is far from the truth.

In the inquiry, the Committee learned that almost 22 per cent of Commonwealth superannuants receive an income from Commonwealth superannuation funds which is less than the maximum age pension of \$11 000 to \$12 000; 65 per cent of superannuants receive less than \$20 000, while 90 per cent receive below \$30 000 per annum. At the same time, while an increasing number receive part age pensions, and so qualify for some cost of living concessions, most Commonwealth superannuants, as self-funded retirees, do not qualify. Moreover, while the majority of Commonwealth superannuants are on low incomes, many fall above the tax threshold, yet they have limited access to tax concessions, and do not have the option of income splitting as do age pensioner couples.

But the central issue was the disparity between the indexation methods used for the age pension and for Commonwealth benefits. The benefit design specifies the use of the Consumer Price Index (CPI) to adjust the value of the benefits on an annual basis. In keeping with the original intention, the CPI as ‘a measure of inflation’ was expected to maintain the ‘real value’ of the benefits. The Australian Bureau of Statistics stated that the CPI is not a measure of the cost of living. Because of the CPI’s proven inadequacy to keep abreast with actual costs of living, the age pension is now adjusted bi-annually through a wage-based indexation mechanism.

Given this, it was the erosion of pensions through the use of the CPI indexation method that became the focal point of the inquiry. The Committee was told that, as a result of its use and the other factors outlined, Commonwealth superannuants form an anomalous group, who fall outside of the safety net provided for age pensioners while sharing their vulnerability. Witnesses reported increasing hardship and difficulty in making ends meet, with many ending up on part age pensions, against all previous expectation.

Accordingly, the report has made recommendations to implement immediately a bi-annual adjustment of the CPI and to consider a phased, alternative indexation method. These measures would build a more consistent framework between arrangements for age pensioners, and those for Commonwealth public sector and defence force personnel.

The inquiry also revealed that the issues raised about the benefit design of Commonwealth schemes were similar to those affecting the members of State-run schemes. The Committee has recommended that, for equity reasons, the changes made to Commonwealth public sector schemes, proposed in this report, also apply to State public sector schemes, where appropriate.

In view of the need for increased consumer education and mechanisms for the orderly transfer of lump sum payments into secure and suitable retirement benefit schemes, the Committee expressed its misgivings about the trend towards the provision of lump sum only payments. The Committee has, over the years, strongly supported the provision of superannuation arrangements that provide a secure income stream for retirees. The report therefore recommends that the current review of the *Superannuation Industry (Supervision) Act 1993* should take this into account.

Finally, the Committee would like to express its appreciation to all those who took part in the inquiry, and particularly to those individual superannuants and State representatives who appeared at public hearings. The Committee is also grateful to the States and Territories who responded to the Committee's survey of State and Territory superannuation schemes.

Senator John Watson

Committee Chair

RECOMMENDATIONS

Recommendation 1—Chapter 3, para 3. 100

The Committee recommends that the Government examine the feasibility of adopting an indexation method other than the Consumer Price Index (CPI) for Commonwealth public sector and defence force superannuation schemes, to more adequately reflect the actual increases in the cost of living.

Recommendation 2—Chapter 3, para 3. 104

The Committee recommends that the Government immediately introduce a bi-annual adjustment of the CPI, which should flow through to Commonwealth public sector and defence force pensions to ameliorate the effects of the current ‘indexation lag’.

Recommendation 3—Chapter 4, para 4. 38

The Committee recommends that, for equity reasons, the changes made to Commonwealth public sector schemes proposed in this report also apply to State public sector schemes, where appropriate.

Recommendation 4—Chapter 4, para. 4. 45

The Committee recommends that the Productivity Commission, in its review of the *Superannuation Industry (Supervision) Act 1993* and related superannuation legislation, should be mindful of the Act’s intention of ensuring that, within a sound prudential framework, superannuation fulfils its role as the preferred savings mechanism by which Australians provide for their retirement.

CHAPTER 1

INTRODUCTION

Background to the inquiry

1.1 In May 2000 the Committee was approached by the National Secretary of the Superannuated Commonwealth Officers Association (SCOA) who wrote expressing the Association's concern that the value of Commonwealth superannuation pensions was being eroded through the sole use of the Consumer Price Index (CPI) to adjust for cost of living increases.

1.2 The Committee subsequently determined that the matter warranted investigation and it sought from the Senate a reference to conduct an inquiry into the benefit design of Commonwealth public sector and defence force unfunded superannuation funds and schemes.

1.3 The detailed terms of reference for the inquiry, which were designed to fully investigate the efficacy of the current indexation arrangements, the rationale for the current method, and the potential of alternative methods, required the Committee to inquire into and report on:

The benefit design of Commonwealth public sector and defence force unfunded superannuation funds and schemes, with particular reference to:

- (a) the method of indexation used by trustees to preserve the real value of fund members' preserved unfunded component of their employer benefit;
- (b) the rationale for using this method;
- (c) the costs and benefits to fund members and trustees of using this method over other alternatives;
- (d) indexation methods used by unfunded and funded state government superannuation schemes where the member's preserved employer benefit remains in the fund;
- (e) the possible implications of adopting another method of indexation; and
- (f) any other issues related to the scope of this inquiry.

1.4 On 8 November 2000, the Senate referred the benefit design of Commonwealth public sector and defence force unfunded superannuation schemes to the Committee for inquiry and report by the last sitting day in March 2001. As the inquiry progressed, some witnesses advised the Committee that they would require several weeks to prepare answers to a number of questions taken on notice. The Committee also determined that it would seek information from the States and

Territories, and that additional time would be needed for their replies to be received. On 6 March, therefore, the Committee sought and was granted an extension of time in which to report to 5 April 2001.

Conduct of the inquiry

1.5 The inquiry was advertised in the *Australian Financial Review* on 17 November, and in the *Weekend Australian* on 18 November 2000, seeking submissions. Details were also posted on the Committee's website. In addition, the Committee wrote to a number of Commonwealth and State superannuation bodies, relevant government departments and bodies, as well as a number of retiree organisations and individuals, inviting submissions.

1.6 The Committee was criticised by some for not advertising the inquiry in the *Canberra Times*, given that Canberra is a city where a number of Commonwealth superannuants reside. Suggestions were made by some that this indicated that the Committee was not intending to conduct the inquiry in an open and honest way. During the course of the inquiry, the Committee responded to these criticisms by pointing out that with national media advertising, and internet advertising, it had made effective use of the resources it has for informing the public of its inquiries. Further, that retired public servants and defence force personnel throughout Australia deserved the same access to information as people in Canberra. It was the Committee's expectation that, having written to a number of retiree organisations, that their members would have been alerted to the inquiry. In responding to some of the criticism in the press, SCOA advised that it and its members were well aware of the Committee's inquiry.

1.7 Notwithstanding that a number of individuals also expressed their concern at not knowing about the inquiry until mid-January, over 180 responded by the due date. Most of these were from Canberra. In total, the Committee received over 200 submissions from Commonwealth and State government departments, public sector and defence force superannuants and a number of major State and Commonwealth superannuant associations. A list of the submissions received is at **Appendix 1**.

1.8 The Committee held Public Hearings on 14 and 15 February 2001. At the hearings the Committee took evidence from officials with policy responsibility in this area—the Department of Defence and the Department of Finance and Administration—as well as from other government bodies such as the Australian Bureau of Statistics (ABS) which briefed the Committee on the preparation of the Consumer Price Index. The Department of the Treasury, responsible for the overarching design of Australia's superannuation policy, was invited to give evidence but declined to appear. So too did bodies responsible for the management and investment of scheme funds, and administration of the schemes: the PSS and CSS Boards, the Defence Force Retirement and Death Benefits (DFRDB) Authority, and the Commonwealth superannuation agency, Comsuper. The last two declined on the grounds that their position as administrators might be compromised.

1.9 To gain an understanding of the views of superannuants, the Committee also invited a number of individual submitters, as well as State and national superannuant groups (representing both civilians and the military), to appear before the Committee to explain their expectations, and criticisms, of the present schemes.

1.10 At the conclusion of the Public Hearing on 15 February 2001, the Committee also provided an opportunity in an open forum for private individuals to make representations to it, to comment on the evidence heard, or simply to tell their own stories. A list of the witnesses who gave evidence to the Committee at the Public Hearings is at **Appendix 2**. A list of the documents tabled at the hearings or received as exhibits is at **Appendix 3**.

1.11 In addition, to aid its understanding of the types and features of various State and Territory superannuation schemes—especially the indexation arrangements which applied, the Committee requested each of the States and the Northern Territory to assist it with its inquiry by providing a response to a questionnaire on their schemes. The Committee did not seek this information from the ACT, as it was advised that employees in the ACT are all covered by the two Commonwealth schemes, the CSS and PSS, and that, while it had plans to offer choice of fund, the ACT Government had no plans to introduce its own scheme.

Main issues arising in the inquiry

1.12 Although the inquiry initially set out to examine the indexation arrangements for the preserved unfunded component of the employer benefit, the main issue which emerged from the evidence to the inquiry was the erosion of the superannuation pension through the use of the present indexation method.

1.13 The Committee was told that, given that Commonwealth superannuants are overall in low income brackets with almost 22 per cent receiving less than the age pension and over 65 per cent receiving less than \$20 000 per annum, the progressive erosion of the value of their pensions must only lead to hardship, undermining pensioners expectations of a ‘reasonable and secure’ retirement.

1.14 The Committee heard that the following factors, along with others such as increased longevity, marriage breakdown and greater mobility in the workplace, are testing the ability of the present benefit of the schemes to meet the expectations of their members, and their needs in retirement.

Unfairness of the indexation method

1.15 The Committee was told that the Consumer Price Index, which is a measure of inflation, does not adequately reflect the rise in the cost of living in the community. This fact, it was argued, is acknowledged by Government in its pegging of the age pension, and parliamentary pensions, to wage-based mechanisms. Commonwealth public sector and defence force superannuants are, therefore, the only members of the retired community whose retirement incomes are tied to growth in inflation, at a time when Government policy aims at low inflation and wages continue to climb.

Lack of relativity

1.16 Related to the above, superannuants who had retired some time ago also noted that, as a result of the CPI indexation of their pensions, their benefits had lost relativity with those individuals retiring at the same rank or level in more recent years. This struck them as particularly unjust.

Loss of selffunded status

1.17 In addition to being unable to keep pace with the cost of living, another focus of concern was that the erosion of the value of their pensions meant that some Commonwealth public sector and defence force superannuants are now in receipt of a part or whole social welfare pension. While some expressed gratitude for this, as it allowed them to keep food on the table, many were deeply disappointed that their independent status as self-funded retirees could not be maintained.

Portability of funds

1.18 More recent retirees were having, or foresaw, financial difficulties because they had been forced to retire early or had been made redundant. Military superannuants were particularly affected, as early retirement is a feature in the defence forces, with length of service now standing at an average of six to ten years (as six years service is mandatory). Under current legislation, this means long years of preservation during which employer contributions are indexed at the CPI rate. As a result of this, some defence force personnel have pressed for fund portability to allow them to roll over the preserved benefit into another complying fund to compound the benefit rather than grow in line with the CPI.

Structure of the report

1.19 These factors fuelled the main complaints against the benefit design of the Commonwealth public sector and defence force schemes: the inadequacy of the CPI to adjust both the pensions and the employer (unfunded) component of the benefits.

1.20 The Committee sought to weigh the views of superannuants against evidence from the departments responsible for policy making in this area and from the ABS; and also to investigate the implications of adopting alternative indexation methods. The Committee also assessed broader issues about the benefit design raised by the inquiry, including the move to funded schemes and fund portability in some State schemes.

1.21 The report comprises four chapters:—

- **Chapter 2:** establishes a context for consideration of the issues that emerged as central to the inquiry. It traces the history of the present benefit design of the Commonwealth public sector and defence force unfunded superannuation schemes, describes their design features, including the rationale for the indexation arrangements, and provides profiles of their membership.

- **Chapter 3:** discusses members' expectations of the benefit design of the schemes and weighs these against official views of the present design. The second part of the chapter explores alternatives to the present indexation method. The immediate and future cost and equity implications for Government and the community if these approaches were to be adopted are then examined.
- **Chapter 4:** provides an overview of the benefit design of State government superannuation schemes, and considers the implications of developments in the States for the benefit design of Commonwealth public sector and defence force unfunded superannuation schemes, both in the short and long term.

Acknowledgments

1.22 The Committee thanks all those who made submissions and/or appeared as witnesses during the inquiry. The Committee was particularly appreciative of the input provided by a large number of individual public servants and defence force personnel, the majority of whom were retirees, who took the time to share their views and experiences with the Committee.

1.23 The Committee also records its appreciation to the States and Territories which responded to the Committee's request for information, as this material contributed greatly to the Committee's understanding of the issues.

1.24 Finally, the Committee would like to thank the Secretariat staff and advisers who assisted in the inquiry. In particular, the Committee would like to thank David Kehl of the Department of the Parliamentary Library Information and Research Service, for his advice and assistance and John Maroney, a former government actuary, now Director of SuperRe Pty Ltd, for his advice.

CHAPTER 2

THE SCHEMES

This chapter establishes a context for consideration of the issues that emerged as central to the inquiry. It traces the history of the present benefit design of the Commonwealth public sector and defence force unfunded superannuation schemes, describes their design features, including the rationale for the indexation arrangements, and provides profiles of their membership.

Benefit design of Commonwealth public sector schemes

2.1 Currently there are two superannuation schemes for the majority of the Commonwealth's civilian employees: the Public Sector Superannuation (PSS) scheme, established in 1990, and the Commonwealth Superannuation Scheme (CSS), which was established in 1976 and closed to new members on 1 July 1990. These schemes replaced their predecessor, the 1922 Commonwealth Superannuation Scheme (CSS).¹

2.2 The benefit design was determined by Government policy, with policy decisions being embodied in legislation enacted by Parliament.² Responsibility for the decision making processes which determine the overarching features of retirement policy is held by the Department of the Treasury, while the benefit design specifications are decided by the Department of Finance and Administration (DOFA).³ The CSS and PSS Boards are responsible for the management and investment of scheme funds, and for administration of the schemes through the Commonwealth superannuation administration agency, Comsuper.⁴

2.3 A key issue under consideration in this inquiry has been whether the present benefit design meets the original intention to 'preserve the real value' of the members' entitlement during retirement. Scheme members referred to the seminal review of the civilian schemes conducted by the Treasurer the Hon. Frank Crean, MP, in 1974, and the review of the Treasurer's proposals by Professor A H Pollard and Mr G L Melville, to provide a context for their views. A sketched history of the present benefit design of the schemes, touching upon the Pollard recommendations, follows.

1 The two schemes cover all Commonwealth employees except those of government business enterprises and other Commonwealth agencies that have separate superannuation schemes for their employees. See Superannuation Bill 1990, Second Reading Speech and Submission No 197, p. 4.

2 Submission Nos 117, p. 1, and 197, p. 4.

3 Submission No 175, p. 1.

4 See Submission No 117, p. 1.

1922 Commonwealth Superannuation Scheme (CSS)

2.4 The first Commonwealth public sector scheme was established by the *Superannuation Act 1922*.⁵ The 1922 Commonwealth Superannuation Scheme (CSS) aimed to provide public servants and their families with a high degree of protection, compared with the majority of the Australian labour force at that time, against adversity arising from member invalidity, death, age retirement, resignation or retrenchment.⁶

2.5 The 1922 CSS provided a defined benefit Pension Scheme and an accumulation Provident Fund. Entry to the Pension Scheme required the employee to pass a medical test after which members paid compulsory contributions, which increased with the life of the membership. Those who had some medical impairment were excluded from the Pension Scheme and became members of the Provident Account, on payment of compulsory contributions of 5 per cent of salary.⁷ No employer contributions were made during the period of membership in the scheme, but pension benefits were payable from the Pension Scheme based on units held, funded in part by members contributions with the remainder from consolidated revenue.⁸

2.6 The scheme was subject to a number of amendments over time, with the main focus of criticism being the contribution structure of the pension scheme, which was based on units of pension accumulated. Under the unit system, contributions as a percentage of salary increased significantly in the later years of service. Thus members over age 40 had often to contribute 25 percent of salary or more to maintain full contributory entitlements. The contributions system was regarded as complex and so complicated administration. The scheme's failure to provide adequate benefits for invalids and the dependents of those who had died while only a short time in service also generated concerns.⁹

Redesigning the 1922 scheme: the Pollard report

2.7 In March 1974, the then Treasurer, the Hon. Frank Crean, MP, announced the Government's proposals for a new superannuation scheme for Australian Government employees.¹⁰ In view of the complexity of the area, it was decided that outside actuarial advice would be sought. Professor A H Pollard and Mr G L Melville,

5 Submission No 197, p. 4, and see Attachment C, p. 21.

6 'Report on the Treasurer's Proposals for a New Superannuation Scheme for Australian Government Employees' (the Pollard Report), June 1974, 1974—Parliamentary Paper No 103, p. 2.

7 Information drawn from Submission No 197, Attachment C, pp. 21–22 and the Pollard Report, pp. 2–3.

8 Submission No 197, Attachment C, p. 22, and background information prepared for the Committee by the Economics, Commerce and Industrial Relations Group, Department of the Parliamentary Library Information and Research Services.

9 See Explanatory Memorandum, Superannuation Bill 1976, pp. 2–3.

10 *The Treasurer's Proposals for A New Superannuation Scheme for Australian Government Employees*, The Treasury, Canberra, March 1974.

Fellows of the Institute of Actuaries, were asked to report on the new proposals. In particular, they were asked to consider the proposals in the light of criticisms of the present scheme, its ‘intended larger and more diverse membership’, as well as those aspects with equity, clarity and cost implications.¹¹ Simplification of the scheme, so that its administration would be easier, and so it could be more readily understood by scheme members was also considered important.¹²

2.8 The Pollard report approved the Treasurer’s proposals overall, commending the Government’s intention to restructure the scheme to provide a lump sum payment in the form of the members’ contributions with interest, to provide full benefits to all members of the service, to allow preservation of benefits after ten years service, and to allow a more flexible contribution scale.¹³ The report also approved generous benefit calculations which would award a pension worth 50 per cent of salary after 40 years of service, but did not endorse the proposed supplementary arrangements bringing the pension to 70 per cent of the final salary.¹⁴

New indexation method

2.9 Recommendation no. 5 of the Pollard report suggested changes to the method of indexation to accommodate the new proposals. Prior to 1973, the pension was indexed on an *ad hoc* basis only. After this time, only the Government funded component of the pension was indexed to increase by 1.4 times the percentage rise in the Consumer Price Index (CPI), provided this did not exceed the percentage increase in Average Weekly Earnings (AWE).¹⁵

2.10 Pollard and Melville saw that the part adjustment of the pension was inappropriate under the proposed scheme, and would result in inequities between recipients. The Pollard report, therefore, recommended that the whole pension should be indexed to the CPI on an annual basis.¹⁶ The adoption of this method was expected to ensure that the benefit was: ‘*not eroded by inflation, but should be adjusted to compensate for the increased cost of living*’.¹⁷ This was judged to be the case even though the CPI was lagging behind the AWE at the time of the review.¹⁸

2.11 From the analysis of Part V of the report, it appears that it was also thought that the application of the CPI to the whole benefit would make pensioners ‘better off’

11 Appendix A, ‘Report on the Treasurer’s Proposals’ 1974, pp. 28–29.

12 Part II, ‘Report on the Treasurer’s Proposals’ 1974, p. 2.

13 See Part IX, ‘Report on the Treasurer’s Proposals’ 1974, p. 25.

14 See Part IV, ‘Report on the Treasurer’s Proposals’ 1974, pp. 7–9. Note: The report did accept the Treasurer’s proposal for 70 per cent pension on invalidity before age 60, but with reversion to the 50 percent pension at retirement age; see p. 10.

15 Part V, ‘Report on the Treasurer’s Proposals’ 1974, p. 14.

16 Part V, ‘Report on the Treasurer’s Proposals’ 1974, p. 16.

17 Part V, ‘Report on the Treasurer’s Proposals’ 1974, p. 13.

18 Part V, ‘Report on the Treasurer’s Proposals’ 1974, p. 14.

because it would rule out the previous requirement that the increase in benefits did not exceed the percentage increase in the AWE.¹⁹ In Part VI, ‘Costs’, the report acknowledged that full indexation to the CPI would result in increased costs to Government of 3.9 per cent per annum, noting that cost estimates were made in respect of existing contributors only.²⁰

1976 Commonwealth Superannuation Scheme (CSS)

2.12 The 1976 CSS Scheme, as implemented, did not reflect the entire benefit design as proposed by the Treasurer in 1974. Coming to power in 1975, the Fraser Government reviewed the proposed scheme and apparently judged it to be too expensive.²¹ Nevertheless, the new scheme aimed to address the main criticisms of the contributions system outlined above and was established by a range of regulations and other instruments under the *Superannuation Act 1976*.²²

2.13 Part X (Clauses 147–153) of the legislation, provided for the Government-financed elements of the pension to be increased annually in July by the percentage increase in the Consumer Price Index over the twelve months ending in the preceding 31 March. The Explanatory Memorandum to the Bill also states that the increases would not apply to the additional contributor-financed pension.²³ No mention was made in explanation of the Bill of the Government’s purpose in applying the CPI method of indexation other than to simplify current measures.²⁴

2.14 According to the Explanatory Memorandum, the Government estimated that, for pensioners and contributors in the existing scheme, the estimated cost to Government in respect of those persons would increase by 1 per cent. It was also estimated that, if the Government liability for benefits were to be funded by the Government making its contribution at the same time as employees, the Government contributions for new contributors entering the existing arrangements under the new scheme, expressed as a percentage of salary would be:

19 Part V, ‘Report on the Treasurer’s Proposals’ 1974, p. 14.

20 Part VI, ‘Report on the Treasurer’s Proposals’ 1974, p. 21.

21 Committee Hansard, p. 65.

22 Attachment B, Submission No 197, p. 17.

23 Explanatory Memorandum, Superannuation Bill 1976, p. 36.

24 See Explanatory Memorandum, p. 44.

	Percentage contribution²⁵
Existing Arrangements (Pension Scheme and Provident Account)	19.5%
New Scheme	18.8%

2.15 The new restructured CSS aimed to cover all employees of the Australian Public Service and related employers, and was established as a partially funded scheme which offered both defined and accumulation benefits.²⁶ These comprised:

- a member component: CSS members made a compulsory contribution of 5 per cent of salary, with options to contribute an additional 5 per cent. A member could receive their contribution as a non-indexed pension or receive it as a lump sum;
- an unfunded employer financed component: paid as an indexed pension (adjusted by the CPI annually) and calculated on factors such as age on leaving, reason for leaving and final salary; and
- a funded employer financed productivity component: usually 3 per cent of salary, paid fortnightly by the employer and receiving interest according to rates determined by the CSS board (usually credit rate interest). The productivity benefit could be deferred, paid as standard pension or rolled over into a complying fund.²⁷

2.16 The notional employer contribution rate (NECR) for the CSS was 21.9 per cent of superannuation salaries.²⁸

2.17 The Scheme was closed to new members on 1 July 1990 with the establishment of the Public Sector Superannuation (PSS) scheme by the *Superannuation Act 1990*.²⁹ However, the CSS remains a complying fund under the SIS legislation and so continues to be eligible to have tax payable on net income of the fund assessed at the concessional rate of 15 per cent.

1990 Public Sector Superannuation Scheme (PSS)

2.18 The PSS scheme is now the only Commonwealth civilian scheme open to new members. It was established by the *Superannuation Act 1990* as a defined benefit

25 Explanatory Memorandum, pp. 6–7.

26 Attachment B, Submission No 197, p. 17.

27 Attachment B, Submission No 197, and background information prepared for the Committee by the Department of the Parliamentary Library Information and Research Services.

28 Attachment B, Submission No 197, p. 20.

29 Submission No 197, p. 4.

superannuation scheme. The PSS remains a complying fund under the SIS legislation and so continues to be eligible to have tax payable on net income of the fund assessed at the concessional rate of 15 per cent.

2.19 The PSS has benefits in two components:

- a member component (the member's contribution and interest): may be paid at rates of between 2 and 10 per cent of superannuation salary, and can be taken as a lump sum up to *SIS Act 1993* limits with the rest preserved in the PSS, or can be wholly preserved in the PSS;
- an employer component (including the productivity benefit): is unfunded, excluding the 3 per cent productivity benefit which is preserved in the scheme until preservation age is reached.³⁰

2.20 The member's contributions and the funded employer component receive credit rate interest, while the employer's unfunded component is indexed to the CPI.³¹ In relation to the indexation method, the Department of Finance and Administration (DOFA) explained that the CPI was adopted as the method of indexation to 'maintain its purchasing power'.³²

2.21 DOFA advised that the primary benefit from the PSS is a lump sum benefit which is calculated by applying the person's benefit accrual to the person's Final Average Salary (FAS)—although half or more of the lump sum benefit may be converted to an indexed pension using age based factors.³³

2.22 Introducing the legislation for the new scheme, the Hawke Government announced that the PSS design made major steps in correcting past inequities in the previous scheme. In particular, it noted that the scheme would offer a choice of lump sum or pension benefits, with the lump sum option now being provided as 'legitimate form of superannuation benefit'. Further, the lump sum option would mean that Commonwealth employees had the same options as private sector employees.³⁴ At the same time, the Government reported significant improvements in resignee entitlements, in that fund members could now choose a preserved benefit option. This would be available as an indexed pension 'at very attractive interest rates'.³⁵

2.23 Commenting on this in its submission, DOFA noted that the CSS had paid a lump sum only (composed of personal contributions and interest) on resignation. The

30 See Submission No 197, pp. 3–4, and 6, and background information prepared for the Committee by the Department of the Parliamentary Library Information and Research Services.

31 Background information prepared for the Committee by the Department of the Parliamentary Library Information and Research Services.

32 Submission No 197, p. 6.

33 Submission No 197, p. 14.

34 Second Reading Speech, Superannuation Bill 1990, p. 1.

35 Second Reading Speech, Superannuation Bill 1990, p. 2.

new PSS arrangements, the Department stated, were in keeping with the spirit of the original design of the PSS scheme, in which preserved benefits were integral.³⁶

DOFA reported, however, that a package of Commonwealth Superannuation Bills currently before the Senate will introduce new superannuation arrangements for Commonwealth employees. The Department explained that the new proposals will ‘provide choice of scheme through a funded arrangement for all new employees and existing CSS and PSS members who choose to leave their schemes’.³⁷ However, under the new arrangements, the proposed new employer contribution level will be reduced to the Superannuation Guarantee level, which is currently 8 per cent.

2.24 At the public hearing, DOFA representatives told the Committee that, as part of the proposal, one set of the Bills would close the PSS.³⁸

CSS and PSS member profiles

2.25 **Table 1**, following, shows the various benefit profiles of members in the major Commonwealth superannuation schemes as at June 2000, provided by the CSS and PSS Boards.³⁹

Table 1: CSS and PSS member profiles

June 2000	CSS	PSS
Contributing members	48 522	112 436
Deferred benefit members	13 879	58 959
Pensioners	109 045	5 714

2.26 A Towers Perrin report (based on membership data at 30 June 1999), projected that:

- the actual Commonwealth Employer Costs are expected to reduce as a percentage of projected GDP from 0.4 per cent in 1999 to 0.2 per cent in 2044;
- the accrued Unfunded Liability at 30 June 1999 for current members and pensioners has been calculated to be \$46 billion, which is 8 per cent of current GDP; and
- the Unfunded Liability will reduce as a percentage of projected GDP over the next 45 years.⁴⁰

36 Submission 197, p. 5.

37 Submission No 197, p. 4.

38 Committee Hansard, p. 131.

39 Submission No 117, p. 2.

Benefit design of the defence force superannuation schemes

2.27 There are two superannuation schemes for the Commonwealth's defence force personnel:

- the Defence Force Retirement and Death Benefits (DFRDB) scheme that was introduced in 1973, replacing the earlier 1948 Defence Forces Retirement Benefits (DFRB) scheme. The DFRDB scheme was closed to new members in 1991; and
- the Military Superannuation and Benefits Scheme (MSBS) which replaced the DFRDB scheme in 1991. All new members of the Australian Defence Force (ADF) are required to be members of the MSBS.⁴¹

2.28 Responsibility for policy oversight of the benefit design of the schemes is carried by the Department of Defence, as determined by the legislation.⁴² The DFRDB Authority is responsible for the general administration of the scheme, subject to direction of Minister, while the MSBS Board of Trustees No.1, manages the MSBS funds.⁴³ Day-to-day administration of the schemes is undertaken by Comsuper.⁴⁴

2.29 A key concern of defence force superannuants is whether the existing schemes extend due reward to Australian servicemen and women for their service to the community by providing adequate retirement incomes commensurate with their expectations, and are comparable to benefits received by other Commonwealth personnel.

2.30 In respect of this, defence force superannuants and representative organisations drew the Committee's attention to the evolution of the schemes. In particular, they referred to the redesign of the 1948 Defence Forces Retirement Benefits (DFRB) scheme on the recommendations outlined in the *Joint Select Committee on Defence Forces Retirement Benefits Legislation Report May 1972*, under Chairmanship of Mr J. D. Jess, CBE, MP.⁴⁵

1948 Defence Forces Retirement Benefits (DFRB) scheme

2.31 The Defence Forces Retirement Benefits (DFRB) legislation was introduced in 1948 following the introduction of a uniform system of pay and allowances for all

40 Towers Perrin, *PSS and CSS Long Term Cost Report*, a report on the long-term cost of the Public Sector Superannuation Scheme and the Commonwealth Superannuation Scheme, 1999, pp. 2–3.

41 Submission No 196, p. [1].

42 Submission No 196, p. [2].

43 See *Defence Force Retirement and Death Benefits Scheme, Annual Report of the DFRDB Authority, 1999–2000*, p. 1, and the *Defence Force Superannuation and Benefits Scheme Annual report of the MSB Board, 1999–2000*, p. 1.

44 Submission No 196, p. [2].

45 ‘Joint Select Committee on Defence Forces Retirement Benefits Legislation Report May 1972’, 1972—*Parliamentary Paper No 74*.

defence force staff in July 1947. The DFRB scheme was designed to meet the special needs of defence force staff, taking into account the design structure of existing Commonwealth public sector schemes.⁴⁶

2.32 The scheme differed from the public sector schemes in a number of respects. In particular, the defence scheme had to take into account the greater variation in retirement age, to respond to rank structure, and to make special provision for invalided staff. Interim arrangements to fund the scheme were also put in place. These remained until 1959 when the scheme became partly funded, consistent with other public sector schemes.⁴⁷

Redesigning the 1948 scheme: the Jess report

2.33 An inquiry was conducted into the DFRB scheme by the Joint Select Committee on Defence Forces Retirement Benefits Legislation after private members and Senators registered concerns about the benefit design of the scheme. In particular, they wished to address the high rate of contributions carried by pre-1959 entrants to the schemes, delays in statutory actuarial reviews, and the growing complexity of the schemes. In keeping with the review of other public sector schemes, the issue of complexity was conjoined with a desire to make the schemes easier for members to understand. After the resolution in the Senate on 2 September 1970, the Prime Minister announced the appointment of Mr Jess as Chairman of the Joint Select Committee for the inquiry, with Mr Crean as the Deputy Chair.⁴⁸

2.34 The Joint Select Committee's report proposed that a new and different scheme should be put in place. The proposed scheme was to be a simplified contributory benefit scheme, and was not to be a funded scheme. It would apply to all members of the Defence Forces and all contributing members would pay 5.5 per cent of pay, with options to make up that amount when transferring from the old schemes. The new scheme would retain the old scheme's feature of commutability, to allow a retiree the option of taking a lump sum, with conditions applying, up to twelve months after retirement. It also specified conditions for payment of annuities to service widows, defacto widows and benefits to children.⁴⁹

Indexation of benefits

2.35 In Recommendation No 6 of its report, the Joint Select Committee determined that the pension, now termed retirement or invalid pay, should be '*expressed as a percentage of final pay and be adjusted annually so that the relativity with average weekly earnings is maintained*'. The recommendation also advised that: 'A possible

46 From Chapter 1, 'Joint Select Committee on Defence Forces Retirement Benefits Legislation' 1972.

47 *ibid.*

48 'Joint Select Committee on Defence Forces Retirement Benefits Legislation' 1972, p. 7.

49 'Joint Select Committee on Defence Forces Retirement Benefits Legislation' 1972 , pp.1–4, and p. 31.

method of achieving this would be to maintain the relativity of benefits to current pay for the rank held on retirement'.⁵⁰

2.36 Discussion of the issue in the report focuses on the relative advantages of the proportion of salary method as against indexation of the benefit to the CPI. The report expressed concerns that inequities may arise using the proportion of salary method, and that it would be cumbersome to administer.⁵¹ At the same time, the report rejected the use of the CPI, which it observed '*does not fairly represent changes in general community standards*'.⁵²

2.37 This conclusion was based on the fact that, at the time of the review, wage increases were running at twice the rate of the CPI. The Joint Select Committee referred the matter to the Department of Defence, pending decisions on the future of service pay, but concluded that regular rather than *ad hoc* indexation of the benefit should take place, and that this should be *related to average weekly earnings* as:

This will ensure that the man in retirement will be able to maintain his position in relation to rising community standards and that he will obtain those increases when they are needed.⁵³

1973 Defence Force Retirement and Death Benefits (DFRDB) scheme

2.38 The Defence Force Retirement and Death Benefits (DFRDB) scheme was established by the Defence Forces Retirement and Death Benefits Act in 1973, but became operational from 1 October 1972, following the Government's consideration of the Jess recommendations.⁵⁴ The new scheme was passed as a suite of Bills designed to simplify the old scheme and correct unsatisfactory features, such as the requirement for high contributions by pre-1959 members.⁵⁵

2.39 Announcing the legislation, the Government pointed out that the new benefit design would allow for commutation of pensions for those retiring after October 1972, that management would be vested in a new statutory authority and reversionary

50 Recommendation No 6, 'Joint Select Committee on Defence Forces Retirement Benefits Legislation' 1972, p. 1.

51 If wages were frozen for any period, or if the changing nature of job specification in the services resulted in 'bizaare results', which would destroy relativity of benefits to different retirees. See 'Joint Select Committee on Defence Forces Retirement Benefits Legislation' 1972, p. 34.

52 Joint Select Committee on Defence Forces Retirement Benefits Legislation' 1972, p. 34.

53 *ibid.*

54 *Annual Report of the DFRDB Authority 1999–2000*, p. 1, and Submission No 196, p. [2].

55 Second Reading Speech, Defence (Parliamentary Candidates) Bill 1973; Defence Force Retirement and Death Benefits Bill 1973; Defence Force Retirement Benefits Bill 1973; Superannuation Bill No (No 2) 1963; and Defence Force Retirement Benefits (Pension Increases) Bill 1973, House of Representatives Hansard, 25 May 1973.

benefits would be extended to defacto widows, with pensions to orphans increased. Invalid arrangements were also revised and an independent appeal Tribunals set up.⁵⁶

2.40 The legislation did not reflect in entirety the Jess recommendations, with the Whitlam Government rejecting indexation to the AWE, and the CPI being adopted.⁵⁷ Announcing the method of adjustment, the Government explained that it was an interim measure to pass on an increase to DFRB pensions, which had not been adjusted since 1971. It was also considered appropriate that there would be consistency with the measures proposed by the new Commonwealth superannuation (CSS) Bill. The legislation therefore proposed that 77.5 per cent of the DFRB pensions would be adjusted ‘in precisely the same manner as the Commonwealth share of superannuation pensions’.⁵⁸

2.41 The DFRDB is an Exempt Public Sector Scheme for the purposes of the *Superannuation Industry (Supervision) Act 1993* (SIS Act), and so is a complying fund under the Income Tax Assessment Act and Superannuation Guarantee (Administration) Act.⁵⁹ The scheme provides superannuation to all Australian Defence Force members who joined after 1 October 1972, and for members of the former DFRB scheme who were compulsorily transferred to the new scheme on that date. The DFRDB continues to provide pensions and benefits to the widows and children of the closed DFRB scheme.⁶⁰

2.42 The DFRDB scheme is an unfunded contributory superannuation scheme. Member contributions are paid into a Consolidated Revenue Fund (CRF), where they do not earn any interest, and benefits are paid from an annual appropriation from the Defence budget.⁶¹ As recommended in the Jess report, the scheme members must make superannuation contributions of 5.5 per cent of fortnightly salary. The superannuation salary is the maximum incremental rate of pay for the member’s rank and includes any Service Allowance payable.⁶²

2.43 Members are entitled to retirement pay after 20 years of effective service, or 15 years if they reached the retiring age for their rank. Entitlements are calculated as a percentage of final salary, with percentages varied by length of service. The member may elect to commute part of retirement pay to a lump sum and receive a

56 Second Reading Speech, Defence (Parliamentary Candidates) Bill 1973.

57 See Attachment 1, Submission No 206.

58 Second Reading Speech, Defence Force Retirement Benefits (Pension Increases) Bill 1973, House Hansard, 25 May 1973.

59 *Annual Report of the DFRDB Authority 1999–2000*, pp 5-6, and see discussion of Heads of Government Agreement in relation to Exemptions in Chapter 3.

60 *Annual Report of the DFRDB Authority 1999–2000*, p. 1, and background information prepared for the Committee by the Department of the Parliamentary Library Information and Research Services.

61 Submission No 196, p. [2].

62 Background information prepared for the Committee by Department of the Parliamentary Library Information and Research Services.

reduced pension. Under part XA of the *Defence Forces Retirement and Death Benefits Act 1973*, and consistent with civilian superannuation models, the pension is indexed annually on 1 July to the CPI for 8 capital cities for the previous March quarter.⁶³

2.44 On resignation before entitlement, a member can receive a resignation benefit as a lump sum of his or her own contributions for transfer to another fund. If a resignee resumes public employment—with the Commonwealth, State or Territory governments and certain bodies established for a public purpose—within a specified period, the resignee may also elect to receive a preserved or deferred benefit.⁶⁴

2.45 A deferred benefit is calculated at the rate of 1.75 per cent of the member's salary for superannuation purposes at the date of the member's discharge for each completed year of effective service in the Defence Force.⁶⁵ The amount will be preserved by the ADF until 20 years of service is completed, during which time it will be indexed at the CPI.⁶⁶

2.46 With the commencement of the MSBS on 1 October 1991, the DFRDB Scheme gave members a one-time option to transfer to the MSBS, or continue in the previous scheme.⁶⁷

1991 Military Superannuation and Benefits Scheme (MSBS)

2.47 The MSBS, established by the *Military Superannuation and Benefits Act 1991*, came into effect on 1 October 1991 following the review of the DFRB scheme by Sir William Cole, with the aim of making the scheme compliant with the *Occupation Superannuation Standards Act 1987* (OSSA).⁶⁸ Announcing the legislation, the Government noted that the new scheme would provide equitable treatment for members of the Defence Force who had served for less than 20 years, and so would be in ‘keeping with community standards’. As well as paying out the member’s contributions on separation, the new scheme would also award interest and a substantial employer benefit, in addition to the 3 per cent productivity benefit.⁶⁹

2.48 The MSBS is a regulated superannuation fund under the SIS Act. It covers all members of the Australian Defence Force (ADF) who joined the services after 1991. As indicated above, the benefits are granted in two components: one funded by the

63 Submission No 196, p. [2].

64 *ibid* and background information prepared for the Committee by Department of the Parliamentary Library Information and Research Services.

65 Background information prepared for the Committee by Department of the Parliamentary Library Information and Research Services.

66 Submission No 196, p. [2].

67 Submission No 196, p. [3].

68 *ibid*.

69 Second Reading Speech, Military Superannuation and Benefits Bill 1991.

employer and the other by the member's contributions.⁷⁰ Members contribute 5 to 10 per cent of their salary each pay into the fund. The member's benefit comprises the member's contributions plus the interest accumulated at the credit rates of the fund.⁷¹

2.49 The MSBS is also different from previous schemes in its intention to pay separating members' benefits as a lump sum. However, to comply with the SIS Act, which superseded OSSA in 1993, only contributions accrued before 30 June 1999 are payable immediately. This means that, despite the scheme's intention to provide a lump sum on separation, member contributions *accruing after 1 July 1999 must be preserved until the member's preservation age*, either in the MSBS, or rolled over to a complying superannuation fund. No part can be converted to a pension.⁷²

2.50 Meanwhile, the employer component, which is largely unfunded and calculated as a defined benefit, is also preserved in the fund until the member turns 55. If a member resigns, the funded component of the employer benefit (the productivity benefit) stays in the MSBS and continues to earn interest at the fund's annual crediting rate. The unfunded component of the employer benefit is fully indexed to the CPI on an annual basis.⁷³

2.51 According to the Department of Defence, the indexation arrangements for both the DFRDB and MSB Schemes recognised a commitment by Government to maintain the purchasing power of the pensions and preserved benefits.⁷⁴

Defence schemes member profiles

DFRB and DFRDB Schemes

2.52 The DFRDB Scheme annual report for 1999–2000 records that the membership of the DFRDB scheme is in decline, falling to 13 341 as at 30 June 2000.⁷⁵ Pay-out in pensions, however, increased to 53 012, and 71 individuals receiving benefits re-entered the ADF in 1999–2000, while some 1 551 members left the scheme. As at June 30 there were 6 774 spouses and 536 children receiving benefits. The report also records that in 1999–2000, 668 invalidity cases were reviewed.⁷⁶ Total benefits paid in 1999–2000 were \$1 039 189.⁷⁷ The following table provides a breakdown of the types of pensions in force at 30 June 2000.⁷⁸

70 Submission No 196, p. [3].

71 *ibid.*

72 Submission No 196, pp. [3–4].

73 *Military Superannuation and Benefits Scheme: Annual Report of the MSB Board, 1999–2000*, p. 1–2.

74 Submission No 196, p. [8].

75 *Annual Report of the DFRDB Authority 1999–2000*, p. 10.

76 *Annual Report of the DFRDB Authority 1999–2000*, pp. 21–24.

77 *Annual Report of the DFRDB Authority 1999–2000*, p. 16.

78 Drawn from *Annual Report of the DFRDB Authority 1999–2000*, p. 21.

Table 2: Pensions in force by type and scheme at 30 June 2000

Type of Pension	DFRB	DFRDB	Total
Retirement	2 192	40 463	42 655
Invalidity	947	2 100	3 047
Reversionary			
—spouses	2 878	3 896	6 774
—children	14	522	536
Act of grace	0	0	0
Total pensions	6 031	46 981	53 012

MSB Scheme

2.53 At 30 June 2000, there were 38 829 contributors to the MSBS, with 32 655 (84.1 per cent) being male and 6 174 (15.9 per cent) being female. The largest number of contributors in 1999–2000 period, at 28.18 per cent of membership, was aged between 20 and 25 years. The next largest group was between 25 and 29 years and comprised 29. 15 per cent of membership.⁷⁹

2.54 The MSB schemes declared interest rates on exit from the MSBS fund ranged between 2 per cent and 15.4 per cent from 2 August 1999 to 26 June 2000. The following table provides a breakdown of exit totals and modes of exit from the fund between 1995–2000.⁸⁰

Table 3: Modes of exit 1995–2000

Mode of Exit	1995–96	1996–97	1997–98	1998–99	1999–2000
Age retirement	84	80	94	81	89
Resignation	4 808	4 065	3 209	3 654	4 084
Redundancy	1	4	64	90	29
Invalidity	435	366	473	653	697
Death	17	19	18	19	12
Other *	251	267	213	243	294
Total	5 596	4 801	4 071	4 740	5 205

*Includes members who had exited but whose applications had not been submitted or were awaiting processing

79 *Annual Report of the MSB Board, 1999–2000*, pp. 23–24.

80 *Annual Report of the MSB Board, 1999–2000*, p. 16; and for Table see p. 25.

2.55 The MSBS report records that the Fund has recorded a good result in a time of financial turbulence, largely due to its investment in the Australian sharemarket which was the best investment sector over the period. At 30 June 2000, fund assets totalled \$996.1million, an increase of 20.3 per cent on the funds under management since 30 June 1999.⁸¹

Conclusion

2.56 The desire to simplify and make more equitable the benefit design of the Commonwealth's civilian and defence force schemes has driven a number of significant reviews of these schemes. The resulting scheme designs, all of which have the pension component linked to an annual CPI adjustment, have worked to address identified inadequacies but, in some incidences, may have given the schemes features which, while consistently applied, may not be in exact sympathy with the intention of the original redesigns.

2.57 In particular, the Committee notes that the Pollard review of 1974, which proposed the introduction of annual indexation of civilian pensions to the CPI, did so in the belief that it would *ensure that benefits would not be eroded by inflation and would be adjusted to compensate for the increased costs of living*. The report also saw that indexation of the whole benefit by the CPI would make pensioners 'better off', in part because it would rule out the previous requirement that the increase in benefits did not exceed the percentage increase in the AWE.

2.58 In contrast to this, in the Jess report in 1972, the Joint Select Committee on Defence Forces Retirement Benefits Legislation rejected the use of the CPI as an indexation method, as it judged that the CPI did not fairly represent '*changes in general community standards*'. This view was arrived at by noting the disparity between the AWE and the CPI at the time of the review. Accordingly, the Joint Select Committee concluded that regular indexation related to AWE would '*ensure that retirees would be able to maintain their position in relation to rising community standards*'. The Jess Committee also pointed to the need to maintain the relativity of benefits to the current pay for the rank held on retirement.

2.59 The Committee considers that analysis of the legislation arising from these reviews does not discount the view that the government did intend to initiate scheme redesigns that would make the schemes more equitable and would improve the benefits to scheme members, in keeping with community standards. However, given the above, it appears that the government, in making its decision to adopt the CPI as the chosen indexation method (compared with a wage-based index, such as AWE or a rank equivalent) may have expected some long-term containment of the cost of benefits.

81 *Annual Report of the MSB Board, 1999–2000*, pp. 10–11.

2.60 In conclusion, it is the Committee's view that an objective of the benefit design of Commonwealth public sector and defence force superannuation schemes was that, with appropriate years of service and contributions, those schemes would ensure that the living standards of retirees kept pace with those of the community by ensuring that the purchasing power of the pensions would be maintained. At the same time, it cannot necessarily be assumed that it was also intended that Commonwealth superannuants would share equally in national productivity gains.

CHAPTER 3

EFFECTIVENESS OF THE SCHEMES

This chapter surveys members' expectations of the benefit design of Commonwealth public sector and defence force unfunded superannuation schemes and weighs these against official views of the present design. The second part of the chapter explores alternatives to the present indexation method. The immediate and future cost and equity implications for Government and the community if these approaches were to be adopted are then examined.

The present benefit design

3.1 In this inquiry, the Committee heard from a wide range of superannuant organisations, representing defence force, public sector and professional groups, and from almost 200 individual superannuants that the present benefit design of the schemes has not met the expectations they had of it in their contributing days.

3.2 RetireInvest, a financial planning organisation with a wide representation of Commonwealth superannuants among its 60 000 clients, reported that, while the overall design of the Government schemes is 'very generous', its Commonwealth clients are uneasy and insecure about their present superannuation arrangements.¹

3.3 Commonwealth superannuant witnesses and submitters reported that this is because current arrangements do not yield security of income, or allow sufficient flexibility to ensure that their benefits will provide adequately for future years in retirement. Against expectation, many found that the value of their pensions had eroded to such a degree that they are now recipients of a part age pension.

3.4 The Superannuated Commonwealth Officers Association (SCOA) explained that its members understood that they had joined a 'genuine career service', and so their compulsory contributions to the Commonwealth superannuation scheme were part of their employment contract. The Committee was told that: 'the contract was that our superannuation would be adequate in retirement'. According to SCOA, the perception is that this *contract has now been broken*.²

3.5 The key reason for this, the Committee heard, is the use of the Consumer Price Index (CPI) to adjust the value of pensions and preserved benefits. This in turn drives dissatisfaction with present arrangements for the preservation of the unfunded component of benefits, both for defence force schemes and under the PSS.

1 Committee Hansard p. 69 and RetireInvest evidence *passim*.

2 Committee Hansard, pp. 10–12.

Adequacy of the present indexation method

3.6 Individual submissions received by the Committee from a wide range of retirees and members in both the Commonwealth public sector and defence force schemes disputed that the CPI is an appropriate indexation method for these schemes. Among responses to the terms of reference, there was consensus overall among Commonwealth superannuant submitters, that:

- a) the method of indexation [the CPI] *does not* preserve the *real value* of fund members' preserved unfunded component;
- b) the rational for applying it appears to be *cost reducing*, as it is at cross purposes with above;
- c) the *costs to fund members* of using the present method *outweighs the benefits*;
- d) relative to funded schemes run by some State governments, *Commonwealth beneficiaries are worse off*;
- e) the use of *alternative indexation* methods would be *more equitable*; and
- f) a major inequity is the *use of the CPI* to index Commonwealth benefits when *other pensions are indexed to wage-based mechanisms*.

CPI—preserving the ‘real value’ of benefits?

3.7 A strong contention of superannuants was that the use of the CPI to index both pensions and preserved benefits does not ‘preserve the real value’ of their benefits. In addition to explaining why and how the CPI method fails to do this (covered under ‘CPI—eroding the value of the benefits’ below) witnesses also sought to explain why they felt this failure was *against the intention* of the original benefit design of the schemes.

3.8 As noted above, superannuants and their representative groups held in evidence to this inquiry that they had a contract, albeit an informal one, with government to provide them with a retirement that was both ‘reasonable and secure’.³

3.9 SCOA, for example, has argued that as the contribution to Commonwealth superannuation schemes was compulsory, it should be viewed as a ‘condition of service not a welfare provision’. SCOA elaborated that superannuation was part of a total package designed to secure the loyalty and expertise of employees’ long term for the government, in lieu of higher salaries available in the private sector. Accordingly, public servants expected that present sacrifice would guarantee them and their

³ Association of Professional Engineers, Scientists and Managers, Australia (APESMA) Submission No 148, p. 1.

families an acceptable standard of living in retirement, or in the event of an employee's disability.⁴

3.10 Members of defence force schemes and their representatives concurred with this, arguing in addition that their sacrifice in having served their country made them doubly distressed at the dismissal of their requests that Government reconsider the indexation method.⁵ As the Australian Council of Public Sector Retiree Organisations (ACSPRO) reported at the public hearing, its affiliates—over one million people: defence force, Commonwealth, State, Territory and member dependants—‘are very disgruntled and disillusioned’ with the present situation.⁶

3.11 In evidence to the Committee the representatives from the Returned and Services League of Australia (RSL) advised that, while the CPI was accepted back in the 1970s, ‘it was a different world’ and that there is a very good case now to look at indexation in terms of what is going on with salaries across other sectors.⁷

Pollard and Jess reports

3.12 Some witnesses referred back to the 1970s reviews, which established the framework for the Commonwealth schemes, to support their claim that Government did, in fact, intend that Commonwealth employees should have income security in retirement as a condition of service.⁸

3.13 As noted in Chapter 2, the Pollard and Jess report recommendations tend to support the view that annual indexation of benefits was adopted to preserve the purchasing power and value of the benefits relative to community standards. Pollard and Jess, for example, state respectively in Recommendations 5 and 6 of their reports that annual indexation of the benefits should compensate for ‘*increases in the cost of living*’ [Pollard]⁹ and should ensure that ‘*the relativity with average weekly earnings is maintained*’ [Jess].¹⁰

3.14 However, the Committee also notes that the Jess report did not see that indexation by the CPI would meet these objectives, and that the Pollard report, while judging that indexation of the whole benefit to the CPI would make members ‘better

4 Submission No 179, p. 11.

5 See for example Submission No 5. The Committee heard that the Australian Council of Public Sector Retiree Organisations (ACSPRO), representing the Regular Defence Force Welfare Association (RDFWA), had made a number of representations on the issue to Government, which had been dismissed. See Committee Hansard, p. 54 and Submission No 206.

6 Committee Hansard, p. 57.

7 Committee Hansard, pp. 84–85.

8 See for example, Committee Hansard, pp. 7; 66.

9 Part V, ‘Report on the Treasurer’s Proposals’ 1974, p. 13.

10 Recommendation No 6, ‘Joint Select Committee on Defence Forces Retirement Benefits Legislation’ 1972, p. 1.

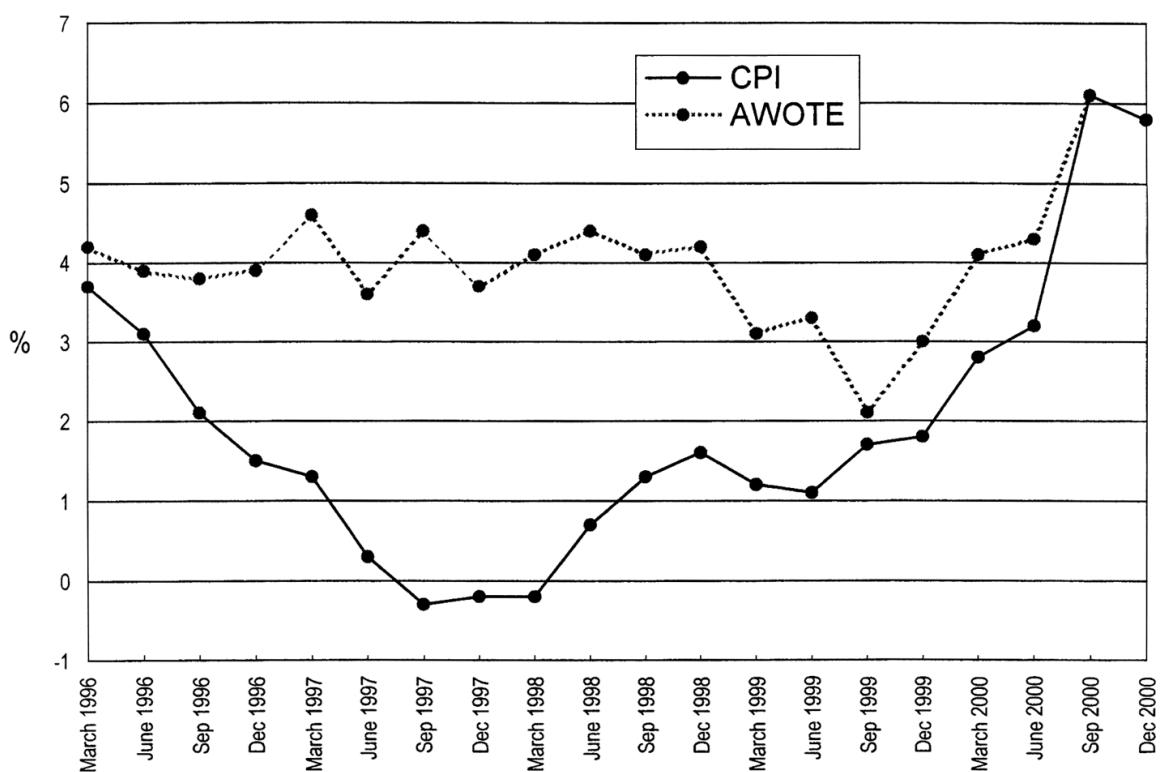
off”, did so when the CPI was lagging behind the AWE.¹¹ As observed in the conclusion to the previous chapter, this appears to suggest that the Commonwealth may have intended to contain the costs of the benefits to some degree by adopting the CPI as the method of indexation for the schemes.

CPI—eroding the value of the benefits

3.15 The Committee received substantial evidence that the value of Commonwealth and defence force superannuants’ retirement incomes has not held pace with the costs of living over the last ten years as a result of the indexation method used.

3.16 The Committee was told that the most obvious indicator of the erosion is the disparity which has existed during that period between increases in the CPI and Average Weekly Ordinary Times Earnings (AWOTE), the measure used to index age pensions). **Table 4** shows this disparity clearly.¹²

Table 4: Comparison of CPI & AWOTE 1996–2000*



*Based on full time average weekly ordinary time earnings (seasonally adjusted)

11 See Part V, ‘Report on the Treasurer’s Proposals’ 1974, p. 14; and Joint Select Committee on Defence Forces Retirement Benefits Legislation’, p. 34.

12 Table drawn from APESMA Submission No 148, p. [4].

3.17 Evidence received by the Committee suggested that the recent merging of the two indices can be partially explained by the introduction of the GST, while the wide variations during the middle of the decade indicate a period of low inflation.¹³

3.18 In providing detail on trends prior to 1996, the Association of Professional, Engineers, Scientists and Managers, Australia (APESMA) pointed out that for much of the decade of the 1990s, AWOTE rates were higher than the CPI, but that there were periods when the CPI was greater.¹⁴

3.19 Witnesses therefore held that the identified disparity between AWOTE and the CPI over this extended period demonstrates the inappropriateness of the CPI, as a measure of inflation, being applied as a cost of living indicator for Commonwealth and defence force superannuation benefits.

3.20 As SCOA reported in its submission, the discrepancy between the two indices meant that in the 10 year period 1990 to 2000, CSS and PSS pensions increased by 24 per cent, based on the movements of the CPI. Meanwhile, over the same period, Average Weekly Earnings (AWE) increased between 37 and 47 per cent, Australian Public Service (APS) salaries on average by 40 per cent and parliamentary pensions by 50 percent. In SCOAs view, this resulted in increased inequities for retirees who are long retired, their benefits losing relativity with those retiring now at equivalent rank and also for women and early retirees.¹⁵

3.21 To gauge the degree of pension erosion SCOA commissioned consultants to survey members' economic circumstances and lifestyle in 2000, as a follow up to a national 1999 survey. The consulting firm, Managing for Productivity, was in the process of conducting a survey of 100 cases. It presented its preliminary findings, based on pilot studies, to the Committee at the public hearing.

3.22 The consultants found that in every case the value of the Comsuper income was being eroded by use of the CPI index, forcing retirees to gradually reduce their standard of living, or to try to plan to do so to avoid future hardship. Some had made detailed records of their expenditure, with one recording a difference of \$2 481 between required and received income after CPI indexation.¹⁶ The firm noted that all interviewees responded that their benefits were not sufficient to support their retirement lifestyle, requiring a range of personal sacrifices.¹⁷

3.23 Managing for Productivity identified a significant trend resulting from these circumstances. The firm found that Australian Public Service (APS) and defence force retirees are increasingly relying on other forms of income, such as the age

13 Committee Hansard, p. 113, and APESMA Supplementary Submission No 203.

14 Submission No 203, p. 2.

15 Submission No 179, p. 2.

16 Committee Hansard, pp. 4–5.

17 Committee Hansard, p. 6.

pension, and either interest from assets or investments, or income from their disposal, to maintain a standard of living or just to survive.¹⁸ The consultants predicted that increasing numbers of lower income households will be forced to receive a part pension and to live more frugally. They concluded: 'If this trend continues, many will become more dependent on the public purse, that is the age pension and public health services'.¹⁹

3.24 The SCOA later advised the Committee that the findings in the final report of Managing for Productivity confirmed that:

...the current indexation system is having a negative impact on the lifestyles in retirement of Commonwealth superannuants. Under current indexation arrangements, Commonwealth superannuation pensions are failing to keep pace with increases in the cost of living and increases in wages. Their standards of living in retirement are falling. Increasingly they are being forced to draw down on savings and investments to support themselves in retirement or to supplement their superannuation pensions by social security benefits.²⁰

3.25 Other witnesses also reported this trend. The National Seniors Association Ltd, for example, stated that on 30 June 2000, with the implementation of the New Tax System, 50 000 self-funded retirees became eligible for part age pensions.²¹ The Combined Pensioners and Superannuants Association of NSW Inc reported that most superannuants had to apply for a part pension because they were 'so hard up'.²² The CPSU saw this movement to part pensions as socially regressive, and argued that reconsideration of the indexation method was crucial.²³

3.26 A number of these witnesses observed that this trend seemed to be at odds with Government policy, which aimed to make individuals less dependent on government assistance and age pensions.²⁴

Rationale of the present indexation method

3.27 At the public hearing, the Australian Bureau of Statistics (ABS) explained the rationale for the compilation of the CPI and what it aims to achieve. The ABS reported that the CPI, as a measure of inflation, is gauged on the basis of price rises on a designated basket of goods; and that the composition of the basket is designed to

18 Committee Hansard p. 4.

19 Committee Hansard, p. 6.

20 Submission No 209, p. 1.

21 Committee Hansard p. 40.

22 Committee Hansard, p. 25.

23 Committee Hansard, p. 18.

24 For example, Committee Hansard p. 26; 54.

represent all but not any one particular household.²⁵ The price on each item is adjusted on an annual basis and the composition of the basket re-weighted on a five yearly basis. The ABS also stated that a number of major reviews of the index have been conducted, such as in 1992 and 1997.²⁶

3.28 ABS representatives emphasised that the adequacy of the index depends on the particular purpose intended.²⁷ They judged that the index was perfectly adequate to gauge the rise in costs of particular items in the basket of goods over a period of assessment. However, ‘to the extent that that fixed basket of goods and services becomes less and less representative of an overall living standard, then the CPI will not pick it.’²⁸ This is because: ‘The CPI is not a measure of the cost of living. It is a measure of inflation and there are differences between the two things’.²⁹

3.29 The ABS concluded that if the purpose was to maintain a relative standard of living with other groups in the community then ‘an earnings measure of some sort’ would be a more appropriate vehicle for indexation.³⁰ Finally, the ABS told the Committee that in weighting the CPI it had to make an ‘on balance’ decision about its primary purpose which, in the end, is a policy issue.³¹

3.30 Evidence from the Department of Defence and the Department of Finance and Administration (DOFA), which carry policy responsibility for the benefit design of the schemes, conveyed the Government’s stance on the issue. Both departments advised that the CPI is ‘used to preserve the real value of the benefits’ and is integral to the original design of the schemes.³²

3.31 In this, the Department of Defence explained, for example, that the CPI indexation is a single component of the scheme design, which also provides other benefits, and should be considered in the context of the overall scheme.³³ DOFA also confirmed that the annual adjustment of the CPI occurs in July, and is based on evaluation conducted in the previous March [for price rises occurring over the previous year].³⁴

25 Committee Hansard, p. 88.

26 See Committee Hansard, ABS evidence 15 February 2000.

27 Committee Hansard, p. 89.

28 Committee Hansard, p. 92.

29 Committee Hansard, p. 89.

30 Committee Hansard, p. 91.

31 Committee Hansard, pp. 93; 98.

32 DOFA Committee Hansard, p. 123 and Submission No 197, pp. 5–6; Defence Submission No 196, p. [8].

33 Committee Hansard, p.133 and Submission No 196, p. [8].

34 Submission No 197, p. 11.

Composition of ‘the basket’

3.32 The Committee heard a number of reasons why superannuant groups believe that the rationale for using the CPI is flawed. One reason is because, as noted above, the CPI is a measure of inflation, and does not keep up with costs resulting from the productivity gains in the community, as reflected by AWOTE. Another important reason, the Committee was told, is because the ‘basket of goods’ used to compile the index by the ABS does not reflect the actual expenses of retirees.³⁵

3.33 A panel of Canberra-based retirees explained that health costs are significant for the retired, including provision of specialist treatment and tests, sometimes requiring medical apparatus or clothing.³⁶ The increased need for household or handyman services also come at a great cost.³⁷ Other increasing expenses include financial services fees, rates and energy costs.³⁸ Fuel and car maintenance costs were also reported as significantly affecting retirees’ ability to continue to make significant contributions to the Australian Capital Territory’s community through volunteer and charity work.³⁹

3.34 Superannuant groups further stated that the CPI does not reflect their living costs as it does not cover first time purchases of such things as computers, mobile phones and electrical appliances.⁴⁰ They also argued that changes to the make-up of the CPI basket over time had rendered it less representative of their needs, such as in the exclusion of interest rates and financial service fees, when many still had mortgages or were renting.⁴¹

3.35 Given the apparent inadequacy of the method as applied to achieve its stated objective, ACS PRO concluded that the Government’s rationale in adopting the method must be to reduce costs to the Commonwealth.⁴²

3.36 The Committee also heard from the Combined Pensioners and Superannuants Association of New South Wales (CPSA), and other superannuant groups, that the present annual indexation results in an ‘indexation lag’ of up to, and between, twelve to fifteen months delay before increases are passed on. Superannuants and

35 Committee Hansard, p. 104.

36 Committee Hansard, p. 102.

37 One witness, for example, reported that the cost to repair a fence had almost trebled in four years, while another noted that over a six year period her pension had increased by only \$87, or about \$14 to \$18 a year. See Committee Hansard, pp. 105; 102.

38 See for example Submission Nos 24, 30, 55, 149 and 160.

39 See for example Submission No 64 and Committee Hansard p. 108.

40 Committee Hansard, p. 55.

41 See Submission No 41 and Committee Hansard, p. 51.

42 Submission No 150, p. 7.

representing organisations saw this as significantly compounding the failure of the current indexation method to ensure pensions meet the needs of the retired.⁴³

Other indexation methods

3.37 In recognition of retiree concerns, the ABS also reported that it is at present compiling some alternative indexes weighted to measure the annual rise in costs of living for different sub-groups, including self-funded retirees.⁴⁴ However, on the basis of the results of similar surveys conducted in 1992, the ABS expected that these would not deliver very different outcomes than the CPI.⁴⁵

3.38 In evidence to the Committee, a number of alternative indices were proposed by superannuants and their representative organisations, and by other bodies. These included:

- ASSIRT Retiree Index—based on the spending patterns of self-funded retirees aged 55 plus and gives a higher weighting to household supplies and services, transportation, recreation and health expenditure;⁴⁶
- AWOTE which, as shown above, charts the average wages growth or MTAWE, male total average weekly earnings; used for age pensions and, in a related mechanism, for parliamentary pensions and the judiciary;
- CPI plus 2 per cent which proposes adjusting up the CPI for disparities between inflation and the cost of living; and
- Fund credit rating, where the unfunded component of the benefit is adjusted to reflect the growth of the managed funds in the PSS or MSBS schemes, as is at present applied to the members' contributions in the schemes.

Indexation of pensions

3.39 Of these methods, AWOTE received strong support in individual submissions protesting pension erosion. There was also some support for CPI plus proposals.⁴⁷ In their submissions, major superannuant organisations SCOA and ACSPRO supported the adoption of a wage-based mechanism.⁴⁸ Given the movements in the two indices

43 See for example Committee Hansard, pp. 26; 55.

44 Committee Hansard, p. 93.

45 Committee Hansard, pp. 91–92.

46 Submission No 179, p. 9.

47 Of alternative indexation methods, most submissions supported application of a wage-based mechanism or, in particular, AWOTE. See for example Submission Nos 9, 10 14, 24 28, 49, 55, 73, 75, 133, 162, 167and 198; and for CPI redesign see for example Submission Nos. 53; 56.

48 Submission No 179, p. 19 and Submission No 150, p. 13.

over the last ten years, as indicated on **Table 4** above, these organisations agreed at hearings that either AWOTE or the CPI, whichever was higher, should be adopted.⁴⁹

3.40 Most witnesses also believed that bi-annual indexation of their benefits would ameliorate some of the inadequacies of the present method. The ABS, which prepares the CPI, reported that it would be feasible to adjust the index more frequently than 5 yearly but there would be costs involved.⁵⁰

3.41 In relation to the possible application of alternative indexation methods to pensions, both DOFA and the Department of Defence reported that work had not been done in this area. Both departments reported that, as policy advisers, they had in fact not been approached about alternative indexation by scheme members.⁵¹ On the instigation of the Committee, DOFA agreed to survey other options and report back.⁵²

3.42 DOFA's response concentrated on the costs of applying the ASSIRT Retiree Price Index relative to the CPI. DOFA explained that as the ASSIRT index is also a measure of inflation, but weighted to reflect assumed spending patterns of self-funded retirees aged 55 and over, the cost of changing from the CPI to this index would depend upon the difference between the Retiree Index and the CPI. DOFA concluded that, based on previous indications, the difference would not be significant.⁵³

Indexation of preserved benefits

3.43 The focus for DOFA and the Department of Defence as policy designers was the alternative proposals for preserved benefits. Both DOFA and the Department of Defence expressed concern about the implications of adopting alternative indexation measures for the benefit design of the schemes, and the increased unfunded liabilities that adoption of these measures might incur.

3.44 In its submission, DOFA stated that the CPI was part of the PSS benefit design and was applied to ensure that no particular advantage would arise to a member who resigned, compared with a person who remained in the service until retirement age. The Department saw that proposals to allow resigning members to roll-over employment benefits could also give rise to preserved benefit members having a particular advantage over contributing members who remained with the PSS until retirement.⁵⁴

49 ACSPRO, Committee Hansard, p. 59, and see also APESMA, Committee Hansard, p. 31.

50 Committee Hansard, pp. 99–100.

51 Committee Hansard, pp. 125; 134.

52 Committee Hansard, pp. 132.

53 Submission No 216.

54 Submission No 197, p. 7.

3.45 The Department of Defence, too, explained that the benefit design of its schemes aims to reward longer term members.⁵⁵ Defence representatives explained that maximum service in the Defence Force was attained at 20 years for most personnel, with people expected to leave active duty at around 40 years of age.⁵⁶ However, the Department reported that there is now a trend for separation from the services at between six and ten years (as six years service is mandatory).⁵⁷

3.46 Under the SIS Act requirements, however, members separating from the defence forces must preserve their unfunded benefits, which are then indexed at the CPI rate until preservation age is reached. Given the long years of preservation, there has been a groundswell of demands for the schemes to be funded, allowing for portability of funds to more lucrative schemes or investments. Complaints against the CPI indexation method of the preserved benefit have been understood by the Department of Defence as related to these demands.⁵⁸

Portability of funds

3.47 Individual submissions from members of defence force schemes partly substantiated the Department's view, with many jointly arguing for the use of a wage-based mechanism for indexation and for portability of funds.⁵⁹ Driven by concerns about the low indexation rates of the CPI, and consequent depreciation of the employer component of preserved benefits over the life of preservation, some scheme members and representing organisations have been pressing Government to provide lump sum payments on separation so that these can be rolled over to complying schemes or investment funds. A related issue was alleged poor management of defence funds.⁶⁰ However, many submitters wrote primarily about the inadequacy of the indexation method.⁶¹

3.48 Representatives from ACSPRO saw that portability of funds was a key issue for members of both defence and civilian schemes.⁶² The CPSU agreed, noting that only those PSS members who are retrenched can roll-over the employer component of their benefits, and so their money is being 'locked away' on a 'uniquely low growth basis'.⁶³

55 Committee Hansard, p. 135.

56 Committee Hansard, p. 137.

57 Committee Hansard, p. 136.

58 Committee Hansard, p. 134.

59 See for example Submission Nos 5, 16 and 17.

60 See for example Submission No 3.

61 See for example Submission Nos 122, 152.

62 As discussed at Submission No 150, pp. 8–9, and Committee Hansard, pp. 49, 51 and 57.

63 See Submission No 146 and Committee Hansard, p. 22.

3.49 In regard to portability issues, the Committee was told that the legislation package currently before the Senate will offer a funded arrangement for all new employees and existing CSS and PSS members who choose to leave their schemes.⁶⁴ The proposed new arrangements will also reduce Government contributions to the Superannuation Guarantee level, which is currently 8 per cent. The Committee also heard that this legislation will not apply to members of the defence force schemes.⁶⁵

3.50 The Committee notes that, as part of the scheduled National Competition Policy Legislation Review, the Productivity Commission has been asked by the Government to undertake a review of the *Superannuation Industry (Supervision) Act 1993* and certain other superannuation related legislation.⁶⁶ Issues relating to portability may be addressed as part of this review.

3.51 Finally, in relation to adoption of an alternative indexation method for both pension and preserved components, ACSPRO proposed that, in order to maintain parity and prevent anomalies arising between them, the same indexation treatment should be applied to both components of the benefit.⁶⁷

Cost implications of alternative measures

3.52 The Committee sought evidence on the cost implications of adopting alternative indexation methods to both the unfunded component of the preserved benefit and the pension itself.

3.53 In its submission, DOFA supplied a table prepared by the actuarial firm Towers Perrin that estimates the comparative costs of applying the different indexation methods to the unfunded component of the PSS preserved benefit. This appears at **Table 5**.

3.54 At the public hearing, DOFA told the Committee that growth estimates for the CPI used by Towers Perrin assumes the CPI would grow by 3.5 per cent per year over the next 40 years, as per the present estimate (to be revised at three year intervals). The design benefit of the PSS as devised in 1990 had been built around that cost structure.⁶⁸

64 Submission No 197, p. 4.

65 Committee Hansard, p. 66, and see Submission No 150, p. 3.

66 ‘Review of the *Superannuation Industry (Supervision) Act 1993* and Certain Other Superannuation Legislation’, *Productivity Commission Circular*, 19 February 2001, No SUPER CI.

67 Committee Hansard, p. 51.

68 Committee Hansard, pp. 126–27.

Table 5: Unfunded liability as at 30 June 1999

Rate of Indexation	Contributory Members (\$b)	Preserved Members (\$b)	Total (\$b)	PSS employer Cost (NECR) ⁶⁹ Percentage superannuation salaries
CPI	3.8	0.7	4.5	14.2%
Crediting Rate	4.3	1.1	5.4	15.7%
AWOTE	4.0	0.8	4.8	14.7%
CPI + 2%	4.1	0.9	5.0	14.9%

3.55 In its submission, DOFA stated that the Budget impact of any change in the method of indexation is likely to be significant and would be an important issue in any consideration of change.⁷⁰

3.56 DOFA further advised that the cost of changing the indexation of 1922 CSS/1976 CSS/1990 PSS pensions to another index will depend upon the differences between the CPI and that index. The Department submitted that:

Based on the unfunded liabilities for those schemes at 30 June 1999, such a change is estimated to increase the present value of those liabilities by around \$6.6 billion if an ongoing 1.5% positive difference is assumed or, by \$4.1 billion if a 1% positive difference is assumed. This costing would apply if, for example, pension indexation changed to MTawe and this index was always 1.5% higher than the CPI.

Also, the average cost of the CSS/PSS could be expected to increase by 2.5% of superannuation salaries if the 1.5% difference is assumed, or 1.5% of superannuation salaries for the 1% assumed difference, all other things being equal.⁷¹

3.57 The Department of Defence, in its submission, also foreshadowed that any indexation changes would significantly increase the costs to government. These would be reflected in Defence departmental appropriations and appropriations administered by the Department of Defence. There would also be a notional interest increase.⁷²

69 NECR: New Entrant Contribution Rate.

70 Submission No 197, p. 7.

71 Submission No 197, p. 12.

72 Submission No 196, p. [8].

3.58 In order to quantify in more detail the estimated costs of applying AWOTE as the indexation method for both Commonwealth public sector and defence force superannuants, the Committee asked both DOFA and the Department of Defence for a detailed break-down of the costs.

3.59 In its response, DOFA estimated that the total budget impact of applying AWOTE to all CSS/PSS pensions and PSS preserved benefits, would be on average \$645 million per year in the four year period from 2001–02 to 2004–05.⁷³ The following table, **Table 6**, breaks down the progression. The detailed breakdown of costs supplied by DOFA is at **Appendix 4**.

3.60 DOFA also advised that the increase in total CSS/PSS unfunded liabilities at 30 June 1999 is estimated to be \$6.9 billion (for CSS/PSS pensions and PSS preserved benefits).

Table 6: Total impact of indexing CSS /PSS pensions and PSS preserved benefits to AWOTE

	2001–02 \$m	2002–03 \$m	2003–04 \$m	2004–05 \$m
Fiscal Balance (Superannuation expenses)	-610	-620	-660	-690
Underlying cash balance The cash balance impacts are based on the MYEFO estimate, including the estimated higher CPI than wage growth in 2000–01 applying to 2001–02 pension payments	50	5	-20	-50
Operating balance	-7510 ⁷⁴	-620	-660	-690

3.61 The Department of Defence advised the Committee that delays had been experienced in obtaining final figures from the Actuary. However, the Department provided figures which were broadly indicative. The estimates indicated that, in general terms, substantial increases in appropriations of between \$150–\$180 million annually to the Defence budget would be needed to fund the cost of applying AWOTE to Defence superannuation schemes. Administered appropriations would amount to approximately \$26 million each year for the increase to the pension and lump sum payments to beneficiaries of the Defence Force superannuation schemes.⁷⁵

73 Submission No 216.

74 Figure indicates the total one-off impact on unfunded liabilities for applying AWOTE to the benefits of the present membership, discounted back to obtain a current figure.

75 Submission No 219.

3.62 The Department also reported that the increase in unfunded liabilities for Defence superannuation schemes would be in the order of \$6 billion, bringing the total of unfunded liability to approximately \$30 billion. It would increase the cost of the schemes by approximately 7–8 per cent, to over 30 per cent, when expressed as an average percentage of salaries.⁷⁶

3.63 The Committee also heard from Australia Post about the implications of adopting alternative measures to the CPI. Australia Post, a funded scheme that took on liabilities from the CSS in 1990, currently uses the CPI to index benefits. It forecast that changing the method to AWOTE would increase Australia Post's liabilities from \$1.2 billion to \$1.4 million, that is, an increase of 16 per cent. Australia Post also expressed concerns that changing the benefit design of the scheme may reward certain members over others, and so would revive issues about the transfer arrangements between the CSS and Australia Post schemes which have since been resolved.⁷⁷

3.64 The SCOA, meanwhile, emphasised to the Committee that whatever costs are incurred through applying an alternative wage-based indexation method, there will also be substantial offsets to those costs—through increased taxation revenues, as well as through reduced pension outlays.⁷⁸ For example, SCOA reported that, in relation to DOFA's estimates that movement from the CPI to a wage-based adjustment for CSS/PSS pensions would add between \$4.1 billion and \$6.6 billion (in gross terms) to long term unfunded liabilities, there would be estimated savings from a taxation ‘clawback’ of between \$1.6 and \$2.5 billion on these liabilities.⁷⁹

3.65 ACSPRO took a similar view of expenses to be incurred through funding preserved benefits on separation, in addition noting that there would be an obvious reduction in future unfunded liabilities.⁸⁰

Future estimates—demographic trends

3.66 Concerns about a potential cost blow out resulting from changes in the age profile of the population was also an issue investigated by the Committee. In relation to this, statistics produced by the ABS, in regard to ageing, and from the Association of Superannuation Funds of Australia (ASFA), in relation to flow on costs in health and pensions, provide a useful point of reference.

3.67 The ABS projects that the number of persons aged 65 and over in Australia will rise from 2.1 million (12 per cent of the population) in 1991 to 2.9 million (13.8 per cent) in 2011, to 4.9 million (20.3 per cent) by 2031. The highest annual rates of

76 ibid.

77 Committee Hansard, p. 75.

78 Committee Hansard, p. 3.

79 Supplementary Submission No 208, p. [2].

80 Committee Hansard, p. 57.

growth among the aged is expected between 2011 and 2021, when the peak number of baby boomers, born in the 20 year period after World War II, move into retirement.⁸¹ This, coupled with the relative drop in birthrates, means that there will be an increased ‘dependency ratio’, with more older people needing to be funded for some 20 years of retirement by a smaller work age population.⁸²

3.68 ASFA records that, in Australia, every aged person costs every State Government 2.3 times the cost of a young person, and this rises to 4.1 times for the Commonwealth Government. At present, some 75 per cent of Australians over age 65 rely on either a full or partial pension as part of their retirement income. The cost to Government in 1998–99, including financial support for war veterans and dependants, was \$18.6 billion.⁸³

3.69 The Government’s Retirement Income Modelling Unit (RIMU) estimates the costs will increase from 3 per cent of GDP in 1998–99 to 3.6 per cent in 2021 and 4.5 percent in 2050, an additional \$2.4 billion, on today’s prices.⁸⁴ RIMU also predicts that health costs will grow at a rate of one per cent a year above inflation, with total government spending on health care rising from a present level of 8 percent on GDP to 9.8 per cent in 2031 and 10.4 per cent in 2041.⁸⁵

3.70 Given these predictions, the Committee sought to clarify how demands for additional funding to present schemes, let alone future ones, could be feasible.

3.71 In a supplementary submission, SCoA challenged the relevance and validity of costing assessments based on demographic change. In particular, SCoA noted that such costings do not take into account predicted growths in GDP. SCoA cited DOFA’s Towers Perrin estimates that the cost of the two government schemes, \$2.4 billion in 2000 (at less than 0.4 percent of GDP), is reducing relative to growth in GDP, and is further predicted to fall from 0.4 per cent in 2000, to 0.2 per cent in 2044.⁸⁶

3.72 Building on this, SCoA also asked the Committee to consider some broader questions about the accounting treatment of superannuation by DOFA. SCoA suggested that accrual accounting over-emphasises the future liabilities of the government schemes, in that payment is in reality incremental, and so does not have to be realised all at one time. SCoA noted that the future liabilities for aged pensions

81 Super Facts: Fact Sheet #1: ‘What’s Age Got To Do With It’, About Super, *ASFA: the Voice of Super* internet site: <http://www.superannuation.asn.au?super>, pp. 1–3.

82 Super Facts: Fact Sheet #1, pp. 2–3.

83 Super Facts: Fact Sheet #1, p. 3.

84 *ibid.*

85 Super Facts: Fact Sheet #1, p. 4.

86 Referring to Towers Perrin, *PSS and CSS Long Term Cost Report*, 1999, p. 23, cited in Submission No 208, p. [3].

are not calculated, and funds are taken out of taxation revenue on a pay as you go basis.⁸⁷

3.73 At hearings, further points were raised about the natural attrition of a number of superannuation schemes and also the effect of downsizing in the public service, which will considerably reduce long-term liabilities for the Commonwealth.⁸⁸

3.74 The National Seniors Association (NSA) also observed that the predicted demographic bulge would, in sixty years time, no longer be an issue and demands for pensions and nursing homes will be in decline.⁸⁹ The NSA also predicted that an ageing society may want more older people in the workforce, to maintain levels of production. This, it saw, would require taxation and other incentives to get people to work beyond 65 and to discourage firms from making people in their fifties and sixties redundant.⁹⁰

Equity implications of alternative measures

3.75 Increased incidence of redundancy, early retirement and mobility in the workforce has also highlighted the deficiencies in the benefit design of the schemes to meet the diverse needs of their members. The Committee noted that, for early retirement and redundancy cases, it is particularly important that the schemes provide benefits which will protect the recipient from hardship by keeping up with living costs, and provide the flexibility to maximise the value of benefit if possible.⁹¹

3.76 Appropriate indexation is the first issue of concern, while flexibility in this context means fund portability—having the ability to roll-over funds into more lucrative schemes or investment funds at a chosen point. RetireInvest, along with ACSPRO and the CPSU saw this as a desirable, if not essential, feature of fund design given the dynamics of the contemporary labour market.⁹²

3.77 Taking note of this, the Committee also sought to consider the ‘intergenerational equity’ implications of the issues before it.⁹³ Demographic trends, for instance, make it clear that the next generation will be working to pay for today’s decisions. That generation may also be subject to less secure employment arrangements. This factor, along with need to equitably share the present pie around, was also taken into account by the Committee.

87 Submission No 208, pp. [3–4].

88 Committee Hansard, p. 114, and pp. 19–20.

89 Committee Hansard, p. 45.

90 Committee Hansard, p. 41.

91 For example, Canberra retiree evidence at Committee Hansard, pp. 139–42.

92 Committee Hansard, pp. 22, 49 and 73.

93 See also Committee Hansard, p. 20.

Relative entitlement

3.78 The Committee understands that age pensioners receive a maximum pension rate of between \$11 000 and \$12 000 a year.⁹⁴ These pensions are indexed twice a year to whichever is the greater of the CPI or MTAWE.⁹⁵ Given that many age pensioners must rely upon a far smaller pension than that received by members of Commonwealth schemes, the Committee invited ACSPRO and other representative organisations to make their case of need compared with age pensioners.

3.79 In this context, ACSPRO, along with individual superannuants, disputed allegations made in the past that Commonwealth superannuants are ‘fat cats’, emphasising that the majority are in fact on low incomes.⁹⁶ To illustrate this point, SCOA in its submission provided the following break up of CSS and PSS pensioner incomes:

- almost 22 per cent receive less than \$10 000;
- 65 per cent receive less than \$20 000;
- over 90 per cent receive less than \$30 000; while
- over 99 per cent receive less than \$50 000.⁹⁷

3.80 The Regular Defence Forces Welfare Association (RDFWA) also told the Committee that many of its members, after 20-year long careers in the armed services, left with \$15 000 and that 40 000 receive less than \$30 000 a year. This group, the RDFWA reported, are slipping further and further behind, and many need income support from the Department of Social Security. This also applies to widows, who receive a mean pension of \$10 000.⁹⁸

Taxation disadvantages

3.81 The Committee heard that, even though most scheme members are low income earners, they are being disadvantaged by the taxation treatment of their benefits compared with benefit recipients in funded schemes, or with age pensioners.

3.82 A number of submissions to the inquiry remarked that the perceived generosity of the various Commonwealth superannuation schemes is offset by the fact

94 Calculated from current weekly benefit rates as listed at the Age Pension link, *Centrelink* internet site: http://wwwcentrelink.gov.au/internet/internet.nsf/payments/age_pension.htm

95 Where the maximum rate is payable and that rate falls below 25 per cent of MTAWE, a top-up of 25 per cent of MTAWE applies. This increase flows through to part age pensions. See Submission No 197, p. 11.

96 Committee Hansard, p. 56.

97 Submission No 179, p. 1.

98 Committee Hansard, p. 54.

that, as unfunded schemes, the benefits received are fully taxed as income.⁹⁹ The CPSU told the Committee at hearings that this is a major concern for CSS and PSS members, who are slipping behind members of funded State schemes. The CPSU explained that, under current legislation, if superannuation benefits come out of a funded scheme they attract a taxation rebate of 15 per cent, thus improving members' PAYE position.¹⁰⁰

3.83 A range of methods to make the taxation of superannuation benefits fairer under current unfunded arrangements were suggested to the Committee. A number of submissions suggested, for example, that there should be taxation relief or supplements to compensate for losses due to the indexation of the benefit to the CPI.¹⁰¹ Another suggestion was that Commonwealth superannuants should have an option for income splitting, which is available to age pensioners.¹⁰²

3.84 The Committee also heard that Commonwealth superannuants felt disadvantaged relative to age pensioners in that, while in the main low income earners, Commonwealth superannuants receive sufficient funds to fall into the lowest tax bracket. This means that, even though their income is minimally above the threshold, they retain their status as self-funded retirees and so have the double disadvantage of having their pension taxed while failing to qualify for any cost of living concessions received by aged pensioners.¹⁰³

3.85 On the other hand, the effect of pension erosion means that increasing numbers of Commonwealth superannuants are now in receipt of a part or whole social welfare pension.¹⁰⁴ The Combined Pensioners and Superannuants Association (CPSA) of New South Wales reported that, for those affected, the loss of an independent income was not only a great disappointment but also meant facing daunting Centrelink income and asset assessments.¹⁰⁵ The CPSA identified the root of the problem as benefit erosion caused by the use of the CPI indexation method, and so argued for 'a fairer benchmark'.¹⁰⁶

An anomalous, and so disadvantaged, group

3.86 A core complaint, expressed widely in evidence to the Committee, was the use of the CPI to adjust Commonwealth pension benefits while the benefits of age pensioners, parliamentarians and the judiciary are adjusted by a wage-based

99 Submission Nos 1, 11, 17 and 65.

100 Committee Hansard, pp. 23–24.

101 See for example, Submission Nos 11, 39 and 60.

102 See for example, Submission Nos 26; 146, and Committee Hansard, p. 37.

103 Such as travel, health and energy discounts. See, for example, Committee Hansard, p. 107.

104 Committee Hansard p. 40.

105 Committee Hansard, p. 25.

106 Committee Hansard, p. 25.

mechanism. This was perceived as quite unfair, if not discriminatory.¹⁰⁷ Commonwealth superannuants were also unhappy about the fact that they were not compensated for the GST, as were other superannuant groups.¹⁰⁸

3.87 The Committee was told that these factors show that Commonwealth and defence force superannuants form an anomalous group, who fall outside of the safety net provided for pensioners while sharing their vulnerability. They feel excluded, not valued as members of the community and, moreover, that the contribution they made during their working lives has been dismissed.¹⁰⁹ As one witness, a scientist and retired public servant argued, the current benefit design is not only inequitable but also suggests that the Australian government does not value achievement. If Commonwealth employees are so poorly rewarded and so poorly regarded, he asked, how can Australia attract and secure the expertise needed for policy, administration and research in the future?¹¹⁰

The plight of the lowest pension groups

3.88 The Committee's attention was also drawn to the injustice of present arrangements for the lowest income groups, including the long-retired, women and early retirees.¹¹¹ The situation of defence force widows was cited as being particularly unfair.¹¹² As noted above, defence force widows receive a mean pension of \$10 000.¹¹³ This is calculated at 62.5 per cent of the deceased member's benefit, lagging behind the APS widow's pension at 67 per cent, and the Parliamentary widow's pension at 83.3 per cent. The RDFWA, in its submission, explained that the widow pension value is further eroded by being notionally indexed to the CPI.¹¹⁴

3.89 In conclusion, individual and superannuant organisations argued strenuously that scheme members, as a group, could not afford to pay the price of poor policy making in the past. At the same time it was agreed that, if a case of relative deprivation was made, any correction to the indexation method could be scaled to assist the lowest income groups first, as this would be the most equitable approach.¹¹⁵

107 See for example Committee Hansard, p. 28, and Submission Nos. 3, 9, 19, 23, 44, 14, 182.

108 See Committee Hansard, p. 112 and, for example, Submission Nos 26, 27, 43, 109, 114, 164, and 186.

109 See Committee Hansard, pp. 104, 107 and 112.

110 Committee Hansard, pp. 103–04.

111 Submission No 179, p. 2.

112 See for example Submission Nos 39; 205.

113 Committee Hansard, p. 54.

114 See Submission No 205.

115 For example, see Committee Hansard, p. 39.

Conclusions and recommendations

3.90 The Committee considers that Commonwealth public sector and defence force superannuants do have grounds on which to claim that they are entitled to a ‘reasonable and secure’ retirement as part of the employment package offered by what was understood to be ‘genuine career service’.

3.91 At the same time, the Committee observes that the legislation itself does not apparently make any such commitment, nor was any binding contract signed—it was instead a founding assumption that, as a condition of service (which required compulsory contributions by employees) the schemes would provide for adequate superannuation in retirement. It was also a founding assumption that, as identified in the Pollard and Jess reports, annual indexation of benefits would preserve the purchasing power and value of the benefits through adequately reflecting the rise in the cost of living.

3.92 Given this, it is nevertheless clear, as revealed by evidence to this inquiry, that the term ‘cost of living’, is not consistently applied. In this regard, the Committee considers that the use of the CPI, as a measure of price indexation, will protect pensioners against inflation of a defined set of goods and services. By contrast, wage indexation will enable pensioners to share in the increased community standard of living from the productivity and economic growth.

3.93 The Committee therefore notes that the expectations of retirees are not being met because the present indexation method appears to be inadequate. Superannuants asserted that this is primarily because:

- the CPI has not preserved the real value of the benefits;
- the CPI has not kept pace with the cost of living;
- the annual adjustments of the CPI result in an indexation lag of 12–15 months, which further erodes the value of the pension;
- the CPI does not keep pace with productivity gains in the community;
- the CPI is not appropriate for retiree expenditure patterns; and
- the CPI has forced reliance on other forms of income such as the age pension.

3.94 The Committee notes the evidence given by the Australian Bureau of Statistics (ABS) that the CPI is not a measure of the cost of living. Rather it is a measure of inflation and, as such, it cannot keep up with costs relative to general community standards of living. The Committee also notes that the ‘basket of goods’ used by the ABS to measure the cost of living does not appear to reflect the actual expenditure patterns of the retired.

3.95 Given the persuasive individual accounts given by Commonwealth and defence force superannuants about the erosion of their living standards through the use

of the CPI, and that this was supported by the study commissioned by SCOA, the Committee has some sympathy for Commonwealth public sector and defence force superannuants who consider that their employment ‘contract’ for a ‘reasonable and secure’ retirement income was legitimate, and that it has been ‘broken’ by the use of the CPI indexation method.

3.96 Taking this into account, the Committee sees merit in the advice of the ABS that, if the purpose of the index is to be used to measure the cost of living, then an index other than the CPI would need to be considered.

3.97 It is therefore the Committee’s view that the CPI alone, as a measure of inflation, may not be the best method to adjust the value of Commonwealth public sector and defence force benefits, if parity with living standards in the community is to be maintained.

3.98 The Committee notes that, by way of comparison, the age pension is linked to the CPI or MTAWE, whichever is the higher, and that adjustments to the age pension occur twice a year.¹¹⁶ The Committee understands that by benchmarking age pensions at 25 per cent of MTAWE the government of the day sought to ensure that pensioners shared in increases in community living standards. This was in recognition of the belief that the CPI alone may not achieve the desired result.¹¹⁷

3.99 To address the situation, the Committee considers that the Government should examine the feasibility of adopting an alternative indexation method that will more adequately reflect the actual rise in the cost of living for retirees relative to community living standards.

Recommendation 1

3.100 The Committee recommends that the Government examine the feasibility of adopting an indexation method other than the CPI for Commonwealth public sector and defence force superannuation schemes, to more adequately reflect the actual increases in the cost of living.

3.101 Where Government considers that the budgetary implications of any changes to the indexation method would be too great, the Committee suggests that the feasibility of the incremental introduction of a phased, two-tier indexation system, as a transitional arrangement, should be examined. Incremental introduction of any change would contain costs for Government, while ensuring that the needs of the lower income groups are met first, as a priority.

116 As a result of changes introduced from 1 July 2000, the 4 per cent supplement to the age pension is indexed to the CPI.

117 Second Reading Speech, Social Security and Veterans’ Affairs Legislation Amendment (Male Total Average Weekly Earnings Benchmark) Bill 1997, House of Representatives Hansard, Wednesday 19 March, 1997, p. 2379.

3.102 The Committee also notes that superannuants find that the present annual adjustment of benefits by the CPI can delay increases to their pensions by some 12 to 15 months, resulting in an ‘indexation lag’ which again reduces the purchasing power of their benefits considerably.

3.103 To address this, the Committee recommends that the Government should, as an interim measure, immediately introduce bi-annual adjustments of the CPI to address ‘indexation lag’ which delays the passing on of increases to the pension benefits of Commonwealth public sector and defence force superannuants. Such a change would make the Commonwealth public sector and defence force arrangements consistent with the arrangements which apply for those on the age pension.

Recommendation 2

3.104 The Committee recommends that the Government immediately introduce a bi-annual adjustment of the CPI, which should flow through to Commonwealth public sector and defence force pensions to ameliorate the effects of the current ‘indexation lag’.

3.105 The Committee notes the variety of suggestions which were put forward as alternatives to the CPI method of indexation and that, of these, there was strong support for changing the method of indexation to a wage-based index, such as Average Weekly Ordinary Time Earnings (AWOTE). At the same time, it was also thought that due to the changing relativities of the CPI and the AWOTE over the last ten years, the preferred method of indexation would be the CPI or AWOTE, whichever is the higher in any year.

3.106 The Committee recognises that the disparity between the CPI and AWOTE over much of the last ten years is the reason why the value of Commonwealth benefits appears to have slipped so far behind. The Committee also acknowledges that Commonwealth superannuants are distressed by the apparent inequity of being the only pensioner group with benefits not being indexed by a wage-based mechanism.

3.107 As a consequence, it is the Committee’s view that the benefit design of the Commonwealth public sector and defence force schemes may not be as equitable in intention as claimed, given that they advocate the application of what has generally been a less remunerative indexation measure, when time has allowed comparative groups to gain through having their benefits linked to productive growth in the community.

3.108 The Committee therefore concludes that there is scope to provide a more consistent framework between arrangements applying to age pensioners, and those applying to Commonwealth public sector and defence force personnel.

3.109 The Committee recognises the special problems faced by those who are required to retire early, for example, due to invalidity. In the interests of equity, the Committee considers that these people should have the superannuation benefit

indexed up to age 60 to AWOTE, as this would enable this group to share in national productivity increases.

3.110 In relation to concerns about the effects of the GST on Commonwealth superannuants, however, the Government does not consider that any inequities have arisen, as compensation for the GST was provided automatically through pension incomes being linked to the CPI.

3.111 The Committee is cognisant that the adoption of alternative indexation measures may incur significant costs to Government that may not be carried by the present overall benefit design of the schemes. In this regard, the Committee notes that, although it would vary from year to year, the total budget impact of applying AWOTE to all Commonwealth public sector and defence force schemes, would be in the order of \$820 million per year and that the total increase in unfunded liabilities would be in the order of \$13 billion. The Committee also notes that demographic developments may also affect the ability of present and future governments to meet a possible blow out in unfunded liabilities.

3.112 At the same time, the Committee is aware that there are contradictory views about the impact that the ageing of the population will have on the long-term costs of Commonwealth superannuation schemes, given the reduced size of the public service and the natural, and assisted, attrition of the schemes. As discussed in the previous chapter, the Committee is also aware that there are projected to be actual reductions in the Commonwealth Employer Costs and in unfunded liabilities over the next 45 years.

3.113 Given this, the Government would need to assess whether isolated changes to scheme designs are financially viable or whether any significant change would require a broader review of the schemes' designs that could enable some financial trade offs.

3.114 The Committee is particularly concerned to ensure that the increase in the number of part pensions does not continue as a significant trend. In this context, the Committee considers that the implications of this trend to part age pensions needs to be carefully assessed. The increase in redundancies and greater career mobility in recent years has fed the trend. The reduction in the age pension taper rate from 50 to 40 per cent is another contributing factor.

3.115 The Committee notes that due to the 40 per cent taper rate, it will always be less expensive for the Commonwealth Government to pay part age pensions to public service and defence pensioners rather than to increase their scheme pensions to avoid paying part age pensions. For example, to eliminate a \$400 part age pension debt would require an additional \$1 000 scheme pension.

3.116 However, in recognition of the significant levels of contributions paid by current Commonwealth pensioners during their working life, the Committee considers it important that these pensioners are provided with an adequate and independent retirement income. This is also consistent with Commonwealth superannuation policy, which encourages retirees to seek independence from the pension.

3.117 Finally, the Committee observes that, with mobility increasing within the workforce, the issue of fund portability has emerged as a significant issue for both Commonwealth public sector and defence force scheme members. In this regard, the Committee is aware that the perceived inadequacy of the indexation method applied to the preserved employer component has exacerbated member dissatisfaction with present arrangements. In addition, the Committee also notes that the current taxation treatment of member benefits in the Commonwealth's unfunded schemes has contributed to this dissatisfaction. The Committee considers that these issues need to be examined further.

CHAPTER 4

THE STATE SCHEMES

This chapter provides an overview of the benefit design of State government superannuation schemes, and considers the implications of developments in the States for the benefit design of Commonwealth public sector and defence force unfunded superannuation schemes, both in the short and long term.

Introduction

4.1 In accordance with the Committee's terms of reference, one of the objectives of this inquiry was to discover how Commonwealth superannuation schemes compare with those offered by State governments; in particular, to compare the methods of indexation applied.

4.2 However, as evidence to the inquiry emerged, with witnesses making a number of comparisons with various aspects of some State schemes, the Committee sought to ascertain information about the broader trends in, and features of, those schemes in order to establish whether there is parity between the benefits available to Commonwealth and State government employees.

4.3 To do this, the Committee wrote to the States and the Northern Territory seeking information about their schemes. The Committee did not write to the ACT as that Territory had advised that its government employees were all covered by Commonwealth schemes, that is either the CSS or PSS, and that the ACT had no plans to introduce its own scheme. The Committee appreciated the cooperation it received from the States and the Northern Territory, as the information provided greatly assisted it in gaining an understanding of the different State and Territory arrangements.

4.4 As noted in the previous chapter, the Commonwealth Government bears the bulk of costs for the aged in the community. The Commonwealth Government has funded an expanding network of welfare payments since 1970, which have absorbed the biggest proportion of the Commonwealth outlays.¹ Aged pensions feature significantly in these outlays, and so the Commonwealth has an interest in ensuring that the benefit design of State superannuation schemes offers genuine retirement schemes that are compliant with the SIS Act.

4.5 In this context, the Committee also sought to clarify the degree to which the development and transformation of the benefit design of some State schemes is consistent with the 'Heads of Government Agreement: Exemption of Certain Public

1 'Social Security Recipients, 1970 to 2000', Department of the Parliamentary Library Information Research Services, *Research Note Number 15, 2000–01*.

Sector Superannuation Schemes from the *Superannuation Industry (Supervision) Industry Act 1993*'.

4.6 Under the Heads of Government Agreement, the States and Territories are required to undertake to ensure that exempted schemes will conform with the principles of the Commonwealth's retirement incomes policy. The major objective of that policy is to ensure an adequate retirement income for all retired Australians. Within this framework all superannuation funds must operate for the purpose of generating and providing genuine retirement benefits for members (or for other purposes consistent with the SIS legislation, including the provision of benefits on death, disability or resignation).

Overview of indexation arrangements

4.7 The Committee sought to identify the indexation arrangements which applied to both the pension and the preserved benefit in State and Territory schemes. In addition to information provided by the States and the Northern Territory, DOFA also provided the following information on its understanding of indexation arrangements for pensions in State schemes, compared with those applied by the Commonwealth.²

Table 6: Pension indexation arrangements for Commonwealth superannuation pensions and superannuation pensions from the main State superannuation schemes

Jurisdiction	Frequency of indexation	Basis
Commonwealth (CSS and PSS)	Annual	All Capital Cities CPI
Commonwealth Military schemes	Annual	All Capital Cities CPI
Queensland	Annual	Brisbane CPI
South Australia	Annual	Adelaide CPI
New South Wales	Annual	Sydney CPI
Tasmania	Bi-annual	All Capital Cities CPI
Victoria	Bi-annual	All Capital Cities CPI
Western Australia	Bi-annual	All Capital Cities CPI

4.8 For the indexation arrangements which apply to the preserved—or deferred—retirement benefit, the picture is not as complete. However, based on the information available to it, the Committee understands that, while the preserved benefits in the Commonwealth schemes are linked to the CPI, the situation in various States is quite different. For example, in NSW the preserved benefits are converted to accumulation

2 Submission No 215.

accounts and accrue at funds earning rates; in Tasmania they are linked to the greater of CPI or AWOTE; while in Queensland, they are linked to AWOTE.

Overview of State and Northern Territory superannuation schemes

4.9 The following table, **Table 7**, provides an overview of the types and features of various schemes based on the information provided to the Committee by the States and the Northern Territory.

4.10 As can be seen from the table, the overall trend is away from unfunded defined benefit schemes, to fully funded accumulation schemes. There is also a trend towards offering employees a choice of fund and investment options. Access to lump sum payments only and fund portability are also major trends.

4.11 Whilst many have undergone major changes in recent years, none of the States indicated that any further changes were proposed.

The move to funded schemes

4.12 The move by States to funded schemes has been welcomed by the Association of Superannuation Funds of Australia (ASFA).³ Commenting on the reported \$8.4 billion in exceptional employer contributions which had been made as one-off payments by State governments to three public sector funds to fund superannuation liabilities, ASFA concluded that this was a ‘good investment’ for governments. ASFA further observed that budget surpluses had allowed the States to alleviate concerns about unfunded superannuation liabilities by ‘giving people choice, and sometimes incentives, to go to accumulation schemes’.⁴

4.13 The Committee heard that the move to funded or part funded schemes had considerably reduced unfunded superannuation commitments in some States.⁵ At the same time, as noted in Chapter 3, under current legislation, if superannuation benefits come out of a funded scheme they also attract a taxation rebate of 15 per cent. Thus, funded schemes offer members the potential of maximising the investment potential of their funds, while also improving their PAYE position.⁶

3 Annabel Hepworth, ‘Governments Deliver Super Efforts’, *Australian Financial Review*, 8 October 1999.

4 Hepworth, ‘Governments Deliver Super Efforts’.

5 See for example Committee Hansard, p. 121.

6 Committee Hansard, p. 23.

Table 7: Types and features of government superannuation schemes in the States and Northern Territory

Type and features	Queensland	South Australia	New Wales	South Tasmania	Victoria	Western Australia	Northern Territory
Defined Benefit schemes	Yes – State, Police and Fire Services schemes are closed	Yes – 4 Police schemes are closed; only Parliamentary and Judges schemes are open	Yes – all closed	Yes – RBF (includes most Police) closed; Fire and Ambulance open	Yes – all closed	Pension Scheme and Lump Sum Scheme are closed	Yes – 3, all closed except members Superannuation Trust
Accumulation schemes	Yes – QSuper is open	Yes – 1 is open	Yes – First Super is only fund open	Yes – TAS is open	Yes – 1 is open – only option since 1994	Yes – 1 is open	No
Hybrid/other schemes	Yes – Defined Benefit account is open	Yes	No	No	No	No	No
Funded/Unfunded	All fully funded	Accumulation scheme is funded; defined benefit schemes are partially funded	FSS is fully funded; benefit schemes partly funded	TAS funded progressively; RBF unfunded	Defined benefit schemes unfunded; SSF has an unfunded portion; accumulation schemes fully funded	Defined benefit schemes partially funded; accumulation scheme is fully funded	2 unfunded; 1 funded
Choice offered	Yes	No	Yes	Yes	Yes accumulation schemes	No	Yes

Continued:

Types and features	Queensland	South Australia	New Wales	South Tasmania	Victoria	Western Australia	Northern Territory
Investment options offered	Yes (five options)	Yes, only in accumulation scheme	Yes (five options)	Yes (five options)	Defined benefit schemes do not provide investment options; ESSS accumulation scheme provides investment options	No – but planning to introduce with effect 1/7/2001	No
Portability available	Yes	Yes, except for the pension schemes	FSS benefits may be rolled out; remaining schemes benefits must generally be preserved but may be rolled out if employer is privatised	Yes	No for defined benefit schemes; Yes for accumulation schemes	No for defined benefit schemes; Yes for accumulation schemes	Yes – on exit of schemes
Access to lump sum	Yes	Yes, in 3 schemes (SLSS, Triple S, Police Lumps Sum Scheme) lump sum only is available; remainder pension and/or lump sum	Yes – all except SSS, PSS and some SASS are lump sum only	Yes – 50% limit has been removed	ESSS provides for lump sum only; SSF and PCSF also provide the opportunity to take the benefits as a pension	NTGPASS Scheme and Accumulation scheme are lump sum only; Pension Scheme can commute share only not State share	lump sum only; Police and LA Members pensions schemes – mixed
Access to death/disability benefits	Yes	Yes	Yes, but different arrangements apply to different funds	Yes – both benefits are offered in all schemes	Yes	Yes	

Continued:

Types and features	Queensland	South Australia	New Wales	Tasmania	Victoria	Western Australia	Northern Territory
Access to compassionate withdrawal of funds	Under certain circumstances	No	Available in FSS; available shortly in remainder	Not while still an employee; preserved benefits may be accessed in accordance with Commonwealth requirements	Yes – following strict guidelines consistent with C'wealth legislation	Yes	Not while member of scheme

Evidence from the States

4.14 In addition to the information gathered from the States reflected above, the Committee received evidence from the Victorian Department of Treasury and Finance and from Victoria's Government Superannuation Office, whose representatives provided an overview of arrangements under its funded schemes. This evidence was complemented by that received the Combined Council of Associations of State Retirees of Victoria.

4.15 The Committee also heard from superannuant organisations based in Tasmania and South Australia, and received a submission from Queensland's superannuation body QSuper.⁷

Victoria's superannuation schemes

4.16 Victoria's largest public sector defined benefits scheme is the State Superannuation Fund (SSF) which is administered by the Government Superannuation Office. The SSF has been closed to new members since 31 December 1993. A revised SSF scheme was closed on 30 June 1998. After 1 January 1994 all new public servants became members of accumulation schemes, and the level of employer support is at the minimum superannuation guarantee level.⁸

Indexation arrangements

4.17 At the public hearing the Victorian Department of Treasury and Finance stated that under Section 91 of the governing legislation, the *State Superannuation Act 1988*, all State pensions must be indexed to the All Capital Cities CPI on a bi-annual basis.

4.18 In response to questions about the possibility of changing its indexation method, the Department reported that the use of CPI indexation is integral to the benefit design of its scheme, and that any changes would result in significant costs to the Victorian tax payer. It stated that it had confidence in the CPI as an adequate indexation method and concluded that, in any case, the Victorian Government has 'other priorities in terms of its scarce resources.'⁹

4.19 The Combined Council of Associations of State Retirees of Victoria argued that one of its main achievements has been the maintenance of the bi-annual CPI in Victoria. However, the Council's representative also pointed out, that even with bi-annual adjustments to the pensions, people at the lower income level were suffering. The Council advised the Committee that the CPI was 'hopelessly out of date,' and that

7 Submission No. 199.

8 Committee Hansard, p. 117.

9 Committee Hansard, p. 118.

to preserve some parity with what they were used to, a more effective index might be to link the pension to a proportion of wages.¹⁰

Portability

4.20 The Department told the Committee that Victoria's new Beneficiary Choice Program will be the first Australian public sector scheme to give members the opportunity to access their preserved benefits as a lump sum.¹¹ The program will offer its 'deferred beneficiaries'—in Commonwealth terms, preserved benefit members—a one-off opportunity to roll-over 50 to 100 per cent of their lump sum to a complying fund of their choice. The Department explained that the amount rolled over will attract a 4 per cent discount per annum (as the lump sum is the indexed benefit which would normally be payable at 55). This discount rate is considered appropriate because future increases in the CPI are expected to be lower than the investment rate.¹²

Access to lump sums

4.21 Meanwhile, under the second component of the program, all new retirees will have the opportunity to commute all of their pension to a lump sum. The program will in part be funded by the \$2.5 billion allocated by the former Kennett Government for privatisation of funds, and part supported by the high level of investment returns yielded by the fund in recent times.¹³

4.22 Responding to this development, the Combined Council of Associations of State Retirees of Victoria drew the Committee's attention to a trend in Victoria for people who have just received a lump sum from VicSuper to spend it hastily or to manipulate their affairs, so that they qualify for the age pension.¹⁴

Reducing unfunded liabilities

4.23 The Department reported that the Victorian Government, through closure of its other schemes and other measures, has succeeded in reducing Victoria's unfunded liabilities from an estimated \$24 to 26 billion down to \$12.5 billion.¹⁵ In doing so, the Committee was told that Victoria had taken a 'major step' in introducing the lump sum and roll-over arrangements as a main feature of its benefit design.¹⁶

10 Committee Hansard pp. 110–11.

11 Committee Hansard, p. 119.

12 Committee Hansard, p. 118.

13 Committee Hansard, pp. 116–17.

14 Committee Hansard, p. 114; 111.

15 Committee Hansard, p. 121.

16 Committee Hansard, p. 121.

Consistency with Heads of Government Agreement

4.24 Questioned about the consistency of its approach with Commonwealth requirements, and in particular, the Heads of Government Agreement on superannuation, the Victorian Department of Treasury and Finance stated its approach was fully consistent with Commonwealth preservation laws, as the lump sums would be rolled over to provide for retirement incomes.¹⁷ The Department's representative also explained that any changes made to the State schemes had to reflect the 'spirit' of the Commonwealth legislation, and must enhance rather than diminish benefits for retirees.¹⁸

Tasmanian and South Australian schemes

4.25 South Australia has two closed schemes and one open. Super SA was closed to new members on 31 May 1986. A lump sum scheme was opened in 1988 and closed to new members on 31 May 1994. Membership in these funds is, naturally, in decline. The Southern State Superannuation Scheme (Triple S) is the only open scheme. Both employer and employee contributions attract credit rate interest in all cases: full preservation, part preservation with roll-over of employee contributions. The CPI is not applied to any preserved benefit and the pension is not applicable.¹⁹

4.26 Tasmania has one closed scheme, the Tasmanian Retirement Benefits Fund, and one open scheme, the Tasmanian Accumulation Scheme (TAS). The closed scheme provides a pension indexed to the All Capital Cities index which is adjusted twice yearly. The preserved benefit, meanwhile, is indexed in line with inflation or the AWOTE, whichever is greater. The Tasmanian Accumulation Scheme comprises member contributions plus Commonwealth SG contributions held in the TAS-SCG account.²⁰ Employer contributions of 8 per cent of salary, will rise to 9 per cent by 2002.²¹ Earnings net fees and taxes are credited to members' accounts. Members can claim a lump sum, allocated pension or a combination at preservation age.²²

4.27 Tasmanian and South Australian representatives appeared with representatives of the Australian Council of Public Sector Retiree Organisations at a public hearing. The representatives urged the Committee to ensure that any beneficial changes arising from changes to the Commonwealth's schemes flowed on to the States and Territories.²³

17 Committee Hansard, p. 119.

18 Committee Hansard, pp. 119–20.

19 Submission No. 150, pp. 10–11.

20 Submission No. 150, pp. 11–12

21 Melanie Alcock, 'Super Funds Go Interstate', *Examiner*, 29 September 2000, p. 5.

22 Submission No. 150, pp. 11–12.

23 Committee Hansard, pp. 57–8.

Q Super—the Queensland State Public Sector Scheme.

4.28 QSuper is a fully funded public sector scheme and features both accumulation and defined benefit accounts. Its schemes provide a range of fund options, utilising a range of investment methods to maximise benefits for recipients.²⁴

4.29 In its submission, QSuper described arrangements for deferred retirement benefits, which feature as part of its defined benefit accounts. It explained that two options are available to resignees, and to ongoing employees who wish to transfer from a defined benefit to an accumulation scheme. These are:

- an Average Wage Option: a default option where the benefit is preserved to 55 years and indexed to AWOTE each quarter. At age 55 the money is transferred to an accumulation scheme where it grows with investment earnings; and
- an Investment Linked Option (ILO): introduced on 1 May 1999, this enables members up to age 55 to convert their Deferred Retirement Benefit (DRB) to a present day value and transfer it to a QSuper accumulation account, where it grows with investment earnings. A choice of five investment options is available ranging from low risk to higher risk returns.

4.30 QSuper reports that a member may roll-over their investment-linked value to another complying super fund of their choice. All money is classified as preserved until SIS preservation age and permanent retirement from the workforce.

Conclusions and recommendations

Parity between Commonwealth and State benefits

4.31 The Committee observes that there is considerable diversity in the method of indexation used by various State schemes, as there is variation in the detail of the overall benefit design of State schemes.

4.32 While all States currently use some form of the CPI to index pensions, there are some State differences, with half of the States using the All Capital Cities index, while the remainder use their own capital city index. Additionally, half of the States adjust the pensions in line with the CPI twice a year, while the other three only make annual adjustments.

4.33 In relation to the indexation arrangements which apply to the preserved, or deferred, retirement benefit, there is even greater diversity between the different practices of the States, and between the States and the Commonwealth.

4.34 In addition to some aspects of the indexation arrangements in some States appearing to be more beneficial than those available to Commonwealth

24 The following information is drawn from QSuper Submission No 199.

superannuants, the Committee notes that a number of State governments offer other design features which could be considered more advantageous. For example, the Committee notes that, through making the most of budget surpluses and effective superannuation fund investment strategies, some States have moved to offer funded superannuation schemes.

4.35 In addition to increasing access to portability of funds, this has enabled these schemes to offer more choice to fund members, while at the same time reducing long term unfunded liabilities. Also, as funded schemes, State superannuants are able to access 15 per cent tax concessions to the total benefit which are unavailable to members of Commonwealth public sector and defence force unfunded superannuation schemes.

4.36 The Committee considers that it would be unfortunate if the benefit design of the Commonwealth schemes allowed members to fall behind members of State schemes, in terms of the generosity of conditions attached to their benefits.

4.37 At the same time, Committee also notes calls from some State superannuants that any improved benefits applying to Commonwealth schemes should flow-on to State arrangements. For equity reasons, the Committee sees it as desirable for any change which might occur in improving the arrangements for Commonwealth schemes (as recommended in the previous chapter) to be reflected in the State schemes, where appropriate.

Recommendation 3

4.38 The Committee recommends that, for equity reasons, the changes made to Commonwealth public sector schemes proposed in this report also apply to State public sector schemes, where appropriate.

Ensuring a retirement income

4.39 Over the years, the Committee has strongly supported the provision of superannuation arrangements that aim to provide a secure retirement income stream for all Australians. Consequently, the Committee has some misgivings about the trend away from the provision of indexed pensions in some State schemes towards lump sum only payments.

4.40 In this regard, the Committee is particularly concerned that the provision of lump sum only benefits will provide an opportunity for ‘double dipping’, where superannuants, having disposed of their lump sum ‘nest egg’ unwisely, or having received certain investment advice, will qualify for the aged pension. This will effectively remove liabilities from State governments and transfer them to the Commonwealth, making responsible long-term planning difficult.

4.41 The Committee acknowledges that there is a trend towards superannuation schemes which offer lump sum only benefits. However, the Committee is concerned that there may not be adequate information available to retirees to sensibly invest their

lump sums to generate income streams and that there may not be sufficient mechanisms to provide for the orderly transfer of lump sums into schemes which could generate a retirement income stream. The Committee considers that the real challenge for both industry and the Government is to provide mechanisms for the orderly transfer of lump sum payments into secure and suitable retirement benefit schemes. This might include making greater use of taxation incentives for people to move into retirement pension arrangements.

4.42 With this background in mind, the Committee has some misgivings about those schemes which provide for a lump sum only, as these schemes may not be giving effect to the spirit of the SIS Act 1993, which requires that benefits are available for genuine retirement purposes.

4.43 At the same time, the Committee also notes that there are some more progressive schemes which aim to look after contributors, not only during their working lives, but also in their retirement years. The Committee applauds these developments and considers that the merits of these schemes should be taken into account in any re-design of Commonwealth public sector and defence force unfunded schemes.

4.44 To address the issue of superannuation providing for retirement, the Committee considers that the Productivity Commission in its inquiry into the SIS Act and related superannuation legislation, should be mindful of the Act's intention of ensuring that, within a sound prudential framework, superannuation fulfils its role as the preferred savings mechanism by which Australians provide for their retirement.

Recommendation 4

4.45 The Committee recommends that the Productivity Commission, in its review of the *Superannuation Industry (Supervision) Act 1993* and related superannuation legislation, should be mindful of the Act's intention of ensuring that, within a sound prudential framework, superannuation fulfils its role as the preferred savings mechanism by which Australians provide for their retirement.

Senator John Watson

Committee Chair

MINORITY REPORT

AUSTRALIAN DEMOCRATS

Senate Select Committee on Superannuation and Financial Services “A Reasonable and Secure Retirement” Minority Report

Senator Lyn Allison

The Australian Democrats welcome this Inquiry. While we are supportive of the general thrust of the majority report, we cannot agree with the overall recommendations. To our mind, there are two key issues with the indexation arrangements for public sector superannuation that need to be considered:

- The appropriate crediting rate for preserved unfunded employer contributions for employees who leave the APS prior to retiring age; and
- The appropriate indexation rate for benefits post retirement.

At present, both preserved employer-funded benefits and post-retirement payments are indexed to CPI.

Indexing of Employer Contributions:

At present, a PSS member’s contributions and the funded employer component receive credit rate interest, while the employer’s unfunded component is indexed to the CPI. DOFA has advised the Committee that using the crediting rate to the unfunded component of the preserved benefit pf the PSS would increase the unfunded liability of the scheme as at 30 June 1999 by about \$900 million. It is uncertain whether this table assumes the crediting rate would be retrospective or prospective.

The issue of the treatment of preserved benefits is of growing importance to APS employees. With growing employee mobility, more and more former employees have amount preserved in the PSS indexed to the CPI. In 1992-93, 78% of separations from the APS were by way of resignation, and only 22% were age retirements. In 1999-200, the percentage of non-age retirements rose to 94%.¹ To put that another way, 94% of people who left the Australian Public Service last year were forced to leave most of their superannuation in a fund where it is earning currently around 2% a year, as opposed to the 10-12% that it could be earning in a private sector scheme.

¹ Public Service and Merit Protection Commissioner Statistical Bulletin

This is, in the view of the Democrats, an indefensible position.

A fundamental principle of superannuation has been that employees should have control over their savings. That means the promotion of portability of benefits – members should be able to move their preserved benefits to where they can earn the best return. To have their employer-funded benefit kept in a fund earning only 2-3% a year until retirement is a form of pensioner robbing in that those people will have less retirement income when they retire.

The current indexation of preserved benefits was introduced in 1990 when the PSS was established by the Hawke Labor Government. The PSS reforms of 1990 contained a number of benefits for employees and were worth doing. However, 1990 was a time of very tight budgets, and it is our understanding that the indexing arrangements were agreed at that time effectively to minimise the cost to the Budget. A decade later, when it is clear that the Commonwealth's unfunded superannuation liabilities are now falling as a percentage of GDP and its Budget surpluses are projected to be quite substantial, the fiscal argument for duding former Commonwealth employees of part of their retirements savings is simply no longer sustainable.

The Democrats recommend:

- That the unfunded employer component of preserved benefits should be credited at the fund's crediting rate effective from 1 July 2001, but not retrospectively;
- That the Commonwealth should consider means of improving the portability of public sector superannuation schemes over time by fully funding employer contributions as they fall due and allowing full portability of such a component.

Indexing of final pension benefits:

The Democrats believe that retirement income policy should, as far as practicable, encourage retirees to take benefits as a pension rather than a lump sum. Implicit in that is ensuring that pension benefits are fair and reasonable.

This Inquiry has heard extensive evidence that the indexing of pensions to the CPI results in inadequate retirement income, particularly given that there is often a 12-15 month delay between major changes in the index and the actual change in the pension rate.

The Democrats support the recommendation of the majority in calling for investigation of better and more appropriate ways of indexing pensions to take into account the cost of living.

We also support the majority recommendation that, as an interim measure, the indexation of the pension should occur more often. Indeed, because of the need to ensure that the pension maintains its spending power, we would recommend that it occur as often as possible, that is, quarterly.

The Democrats recommend:

That public sector superannuation pensions be indexed quarterly to movements in the CPI, and investigations be conducted on identifying an index that better reflects the cost of living for aged pensioners.

Lyn Allison

Democrats Committee Member

APPENDIX 1

LIST OF SUBMISSIONS

Submission No.	Submittor
1	Mr Robert Neill
2	Mr M J Cribbin
3	Mr Stuart Friend
4	Mr Peter Jordan & Mrs Geraldine Jordan
5	Mr Brian Werndly
6	Mr Peter Glover ANZIM
7	Mr Graham Barnard
8	Mr Kerry Burgess JP
9	Mr Colin Fleming
10	Mr Mark McDonough
11	Mr Harold Chandler
12	Mr Tony Foord
13	Mr Murray Upton
14	Mr Allan Dent
15	Mr Francis McKone & Mrs Margaret McKone
16	Mr Christopher Sullivan, WGCDR Ret'd
17	SQNLD R Martin Smith
18	Mr Denis Wilson AM
19	Ms Julianne Kamprad
20	Mr G F Tearle
21	Mr Nick Philippa

- 22 Mr Jack Marshall
- 23 Mr David Wilson & Mrs Elizabeth Wilson
- 24 Mr Barry Leyshan
- 25 Mr Max Ellem
- 26 Mr Joseph Clark
- 27 Mr Horst Kuessner & Mrs Denise Kuessner
- 28 Mr Clifford Johnston
- 29 Confidential
- 30 Mr Clive Williams
- 31 Mr Richard Willimott
- 32 Mr Brian Sankey
- 33 Mr Christopher Packham
- 34 Mr Graeme Secker
- 35 Mr Bevin Wood
- 36 Mr Ron May
- 37 RetireInvest
- 38 Dr Kay Lindsay
- 39 Mr C G Harvey, Group Captain Ret'd
- 40 Mr Noel Matthews
- 41 Mr L R Rayner
- 42 Mr B R Adams
- 43 Mr Brian McNamara
- 44 Mr Michael Coughlan
- 45 Mr K B Keeling
- 46 Name withheld

47	Mr Malcolm Dubois
48	Mr Graeme Halprin
49	Mr Glyn Price
50	Mr Rod Foster
51	Mr E A Hingee
52	Mr P Ryan
53	Emeritus Professor Ralph Slatyer AC
54	Mr Edward J Burke
55	Mr Graham Bailey
56	Mrs J A Laraman
57	Mr Graham Pope
58	Mr A E Kyburz
59	Mr John Morland
60	Mr Keith Love
61	Dr Phil McFadden
62	Mr Peter F Crapper
63	Mr Colin Dennett
64	Mr K B Flynn
65	Miss D J Williams
66	P B Carton
67	Name withheld
68	Mr David V Pedersen
69	R Reichelt
70	Ms Robina McCaffrey
71	Name withheld

72	Mr Neville Apps
73	Mr Warren Butler
74	Ms Desma Butler
75	Mr Ian Ridgway & Ms Joan Silins
76	Mr John Muchmore
77	Name withheld
78	Name withheld
79	Mr Paul Johnson
80	Name withheld
81	Mr Basil Bautovich
82	Australia Post, Vic
83	Mr Lee Harris
84	Mr Mike Lynch
85	Mr T F Holm
86	Mr Geoff Olney
87	Name withheld
88	Mr Peter Hopgood
89	Mr Robert Kyle
90	Colonel P A Bysouth, AM DFC
91	Mr Peter Adnams
92	Ms Julie Lindner
93	Mr Robert Ward
94	Mr D J Sheaves
95	Mr M D Garbutt
96	Mr Trevor Nock

- 97 Mr Des Broom
98 Mr Gregory Freeman
99 Name withheld
100 Mr Shane Layt, WO2 RAEME (Ret'd)
101 Mr Robert Foster
102 J A Harnett
103 Mr David Roberts and Mrs Jospehine Roberts
104 Mr Shane Rashleigh
105 Mr Douglas Batten and Mrs Jill Batten
106 Mr Mike Castle
107 Mr Anthony Siracusa
108 Mr S G Smith
109 Ms Coralie Walker
110 Mr Barry Walker
111 Mr Keith Bailey
112 Mr M A Park
113 Mr William F Schleiger, Group Captain (Ret'd)
114 Ms Sue Kesteven
115 Mr Kevin Jennings SGT MTD2 RAAF (Ret'd)
116 Mr Geoff J Hall, Group Captain (Ret'd)
117 CSS & PSS Boards
118 Sixto Diaz
119 Mr Jeffrey Leeke
120 National Seniors Association
121 Mr Michael Welch

- 122 Mr P J Burn, CMDR RAN (Ret'd)
- 123 Ms Audrey Guy
- 124 E Kiiver
- 125 Ms Roseanne Toohey
- 126 Mr Sam Molloy
- 127 Mr Bill Egan
- 128 Mr A C Stevenson
- 129 Mr Paul Appleby
- 130 Mr Richard Robinson
- 131 Mr Tom Mitchell
- 132 Mr R Bergsma
- 133 Mr James Smith
- 134 Clovis Mendes
- 135 Ms Gwenda Bramley
- 136 Mr Jeff Sharrad
- 137 Ms Mary Voice
- 138 Mr Peter Trevithick
- 139 Mr Ray Thomas, Warrant Officer (Ret'd)
- 140 Mr W W Reading
- 141 Mr Barry Wilson
- 142 Glenn Hilling
- 143 Mr David Hine
- 144 Mr Gary Holdges
- 145 Confidential
- 146 Commonwealth and Public Sector Union (CPSU)

- 147 Mr Colin Johnson
- 148 Joint submission from the Association of Professional Engineers, Scientists & Managers, Australia (APESMA), and
the Professional Officers Association of Victoria (POAV)
- 149 Mr David Banks
- 150 Australian Council of Public Sector Retiree Organisations Inc (ACPSRO)
- 151 Mr D Callaghan
- 152 R J Salmond
- 153 Mr John Reavell
- 154 T A J Keays
- 155 Mr Robert C Moore
- 156 Mr Patrick Donnelly
- 157 Ms Patricia Dalton
- 158 Ms Claire Southwell
- 159 J L Baker
- 160 Mr Erik Wilson
- 161 Mr Arthur Fielden
- 162 Mr Rod Foster
- 163 Ms Monica McNamara
- 164 Mr John Leane
- 165 Mr Colin Fuller
- 166 Mr Barrie Pennefather
- 167 W B Rotsey
- 168 Mr Ian Cook

- 169 Combined Council of Associations of State Retirees in Victoria
- 170 Ms Hazel Arnold
- 171 Mr David Edwards PSM
- 172 Mr John Pye
- 173 Mr Raymond Casley-Smith JP
- 174 Returned & Services League of Australia Limited (RSL)
- 175 Treasury
- 176 Dr David Hanson
- 177 Mr Barrie Smith
- 178 Association of Independent Retirees, Inc
- 179 Superannuated Commonwealth Officers' Association (Federal Council) Inc (SCOA)
- 180 Joint submission from Combined Pensioners & Superannuants Association of NSW Inc (CPSA), and Australian Pensioners' and Superannuants' Federation of Australia (AP&SF)
- 181 Lin Stock
- 182 Mr I D Yeaman
- 183 Mr David Joicey
- 184 Tasmanian Association of State Superannuants
- 185 National Seniors Association
- 186 Mr James Kelly
- 187 Mr Simon Fisk
- 188 Australian Council of Trade Unions (ACTU)
- 189 Mr Ray Merchant
- 190 Mr David Dunnet

- 191 Mr K Trescher
- 192 Mr Kommer Springvloed
- 193 Mr Robert J Kyle
- 194 Mr John E Miller
- 195 Mr Norman Knowles
- 196 Department of Defence
- 197 Department of Finance and Administration
- 198 Armed Forces Federation of Australia
- 199 QSuper
- 200 Wing Commander Lindsay Williamson
- 201 Mr Graham Bailey
- 202 Victorian Department of Treasury and Finance
- 203 Association of Professional, Engineers, Scientists & Managers, Australia (APESMA), and Professional Officers Association of Victoria (POAV) (Supplementary Submission)
- 204 Professor Harry Green
- 205 Regular Defence Force Welfare Association Inc (RDFWA)
- 206 Regular Defence Force Welfare Association Inc (RDFWA) (Supplementary Submission)
- 207 Mr J V McMahon (Supplementary Submission)
- 208 Superannuated Commonwealth Officers' Association (SCOA) (Supplementary Submision)
- 209 Superannuated Commonwealth Officers' Association (SCOA) (Supplementary Submision)
- 210 Premier's Department, New South Wales
- 211 Department of Treasury and Finance, Tas
- 212 QSuper

- 213 Super SA
- 214 Northern Territory Superannuation Office
- 215 Department of Finance and Administration
- 216 Department of Finance and Administration
(Supplementary Submission)
- 217 Government Employees Superannuation Board, WA
- 218 Confidential
- 219 Department of Defence

APPENDIX 2

WITNESSES WHO APPEARED BEFORE THE COMMITTEE AT PUBLIC HEARINGS

Wednesday, 14 February 2001, Canberra

Superannuated Commonwealth Officers Association

Ms Helen Allnutt, National Secretary
Mr John Brigg, National President
Mr Terry Fawl, National Vice-President
Mr Peter Hurley, National Vice-President

Managing for Productivity

Ms Kris Newton, Consultant
Mr Neil Taylor, Managing Proprietor

Community and Public Sector Union

Mr Sandy Ross, Secretary, CSIRO Staff Association;
Member, National Management Committee, CPSU
Mr Noel Speers, Industrial Organiser

Combined Pensioners and Superannuants Association of NSW Inc.

Mr Colin Knights, Member, State Executive
Mr Raymond Merchant, Assistant State Secretary
Mr Gerard Thomas, Policy Officer

*Association of Professional Engineers, Scientists and Managers, Australia; and
Professional Officers Association (Victoria)*

Mr Bernard Parsons, Senior Industrial Officer

National Seniors Association Ltd

Mr David Deans, Chief Executive

Regular Defence Force Welfare Association

Commodore Harold Adams, National President

Australian Council of Public Sector Retiree Organisations Inc

Mr Gordon Johnson, National President

Mr Frank Morony, President, South Australian Superannuants

Air Vice Marshall John Paule (Retired), National Secretary

Mr Anthony Robinson, Executive Member, Tasmanian Association of
State Superannuants

RetireInvest Pty Ltd

Miss Jennifer Brookhouse, Technical Manager

Australia Post

Mr Angus McKenzie, Group Manager, Superannuation

Returned and Services League of Australia

Major General Peter Phillips, AO, MC (Retired), National President
 Brigadier James Townley, AM (Retired), Chairman, National
 Conditions of Service Committee

Thursday, 15 February 2001, Canberra*Australian Bureau of Statistics*

Mr Garth Bode, Labour Statistics Branch
 Mr Peter Harper, First Assistant Statistician, Economic Accounts
 Division
 Mr Stephen Whennan, Assistant Director, Consumer Price Index
 Section

Ms Gwenda Bramley (Private capacity)

Mr Michael Coghlan (Private capacity)

Mr Lennard Dyer (Private capacity)

Mr Keith Flynn (Private capacity)

Dr John Lindsay (Private capacity)

Mrs Monica McNamara (Private capacity)

Combined Council of Associations of State Retirees of Victoria

Mr Lindsay Whitrod

Government Superannuation Office (Victoria)

Mr Mario Maddalena, Information Technology Project Officer

Victorian Department of Treasury and Finance

Mr Dean Yates, Assistant Director, Superannuation

Department of Finance and Administration

Mr Alastair Hodgson, General Manager, Business Services Group

Mrs Rosemary Robinson, Director, Policy/Legislation and

Governance, Superannuation Branch

Ms Sandra Wilson, Branch Manager, Superannuation Branch,

Business Services Group

Department of Defence

Mr Phillip Charley, Director, Superannuation

Group Captain Lee Roberts, Director, Salary and Allowances

Mr Adrian Wellspring, Director-General, Personnel Policy and

Employment Conditions

Mr Etienne Hingee (Private capacity)

Mr Trevor Smith (Private capacity)

Mr Kevin Wilkinson (Private capacity)

APPENDIX 3

TABLED DOCUMENTS/EXHIBITS

1. Report submitted by Leon Bubenicek, RAAF Williamtown, by the Armed Forces Federation of Australia, *MSBS and the Rights of ADF Members - a Perception of Discrimination*, August 2000.
2. *PSS and CSS Long Term Cost Report*, a report on the long term cost of the Public Sector Superannuation Scheme and the Commonwealth Super Scheme 1999, Towers Perrin, provided by Superannuated Commonwealth Officers Association at the Public Hearing on 14 February 2001.
3. *A Guide to the Consumer Price Index*, 14th Series, Australian Bureau of Statistics, December 2000. Tabled by the Australian Bureau of Statistics at the Public Hearing on 15 February 2001.
4. Extract from *Report of the Defence Force Retirement and Death Benefit Scheme Review Committee* (Cole Report), provided by the Department of Defence at the Public Hearing on 15 February 2001.
5. Information Paper *An Analytical Framework for Price Indexes in Australia*, February 1997, provided by the Australian Bureau of Statistics, 23 February 2001.
6. Information Paper *Issues to be Considered During the 13th Series Australian Consumer Price Index Review*, May 1997, provided by the Australian Bureau of Statistics, 23 February 2001.
7. Information Paper, *Outcome of the 13th Series Australian Consumer Price Index Review*, November 1997, provided by the Australian Bureau of Statistics, 23 February 2001.
8. Information Paper, *Price Indexes and the New Tax System*, May 2000, provided by the Australian Bureau of Statistics, 23 February 2001.
9. Information Paper, *Introduction of the 14th Series Australian Consumer Price Index*, September 2000, provided by the Australian Bureau of Statistics, 23 February 2001.
10. Information Paper, *The Australian Consumer Price Index, Feasibility of Constructing Price Indexes for Special Population Groups*, February 1992, provided by the Australian Bureau of Statistics, 23 February 2001.
11. Feature Article, *Experimental Price Indexes for Age Pension Households: An Update*, January 2000, provided by the Australian Bureau of Statistics, 23 February 2001.

12. *Consumer Price Index - Population Subgroup Indexes*, provided by the Australian Bureau of Statistics, 23 February 2001.
 13. *Movements in the CPI Between June Quarter 1997 and March Quarter 1998*, provided by the Australian Bureau of Statistics, 23 February 2001.
 14. *Implication of Removing Mortgage Interest and Consumer Credit Charges from the CPI*, provided by the Australian Bureau of Statistics, 23 February 2001.

APPENDIX 4

DEPARTMENT OF FINANCE AND ADMINISTRATION RESPONSES TO QUESTIONS ON NOTICE

(SUBMISSION NO 216)

1. Cost of applying AWOTE to:

- (a) superannuants who retired due to invalidity both up to age 60 then CPI beyond and AWOTE for total retirement period;**
- (b) superannuants who retire early, ie before age 60, cost of AWOTE then application of CPI after age 60;**
- (c) superannuants, applying AWOTE in the following categories:**
 - receiving less than \$10,000 a year
 - receiving less than \$15,000 a year
 - receiving less than \$20,000 a year

and so on in levels of \$5,000 up to \$60,000.

2. Total cost of applying AWOTE to all public sector personnel

3 What is the estimated budget impact, not as a percentage of GDP, of applying AWOTE to all public sector funds for all civilian personnel over the next budget period, including forward estimates?

4. Use of other indexes such as the ASSIRT Retiree Price Index

ANSWERS

	Increase in CSS/PSS employer contribution rates (% of super salaries) as at 30 June 1999.		Increase in total CSS/PSS unfunded liabilities as at 30 June 1999
	CSS	PSS	(\$'billion).
Q1(a) (Invalidity retirees)			
- AWOTE to age 60	0.1%	0.1%	0.2
- AWOTE for total retirement period	0.2%	0.2%	1.0
Most CSS and PSS members who are retired on invalidity grounds and take a pension will, unlike a person retiring early for any other purpose, receive not only their accrued entitlements at the time of retirement but also recognition for service not completed (ie prospective service) because they retired early. This means in the case of the CSS for example that a person retiring on invalidity at age 40 with 15 years service gets an indexed pension of 50% of salary whereas a person made redundant in these circumstances and taking a pension would only be entitled to 9% of salary.			
Q1 (b)(Early retirees)			
- AWOTE to age 60	0.2%	0.1%	0.2
Q1(c)			
- AWOTE up to \$10,000 / year	0.1%	0.7%	0.5
- AWOTE up to \$15,000 / year	0.3%	0.9%	1.2
- AWOTE up to \$20,000 / year	0.4%	1.1%	2.0
- AWOTE up to \$25,000 / year	0.8%	1.4%	2.9
- AWOTE up to \$30,000 / year	1.2%	1.6%	3.8
- AWOTE up to \$35,000 / year	1.7%	1.6%	4.4
- AWOTE up to \$40,000 / year	2.2%	1.7%	5.0
- AWOTE up to \$45,000 / year	2.5%	1.7%	5.4
- AWOTE up to \$50,000 / year	2.9%	1.7%	5.9
- AWOTE up to \$55,000 / year	3.1%	1.8%	6.1
- AWOTE up to \$60,000 / year	3.3%	1.8%	6.2
Q2 (All pensions and PSS unfunded preserved benefits)			
AWOTE – all pensions	3.7%	1.8%	6.6
AWOTE – PSS preserved benefits		0.5%	0.3

Note – These estimates relate to scheme costs only, they take no account of increased administrative costs arising from applying different levels of indexation to certain categories of CSS/PSS pensioners.

Q3 What is the estimated budget impact, not as a percentage of GDP, of applying AWOTE to all public sector funds for all civilian personnel over the next budget period, including forward estimates?

TOTAL IMPACT OF INDEXING CSS/PSS PENSIONS AND PSS PRESERVERS AT AWOTE				
	2001-02	2002-03	2003-04	2004-05
	\$m	\$m	\$m	\$m
Fiscal balance (superannuation expenses)	-610	-620	-660	-690
Underlying cash balance. The cash balance impacts are based on the MYEFO estimate, including the estimated higher CPI than wage growth in 2000-01 applying to 2001-02 pension payments.	50	5	-20	-50
<i>Operating balance</i>	-7510	-620	-660	-690

Q4. Use of other indexes such as the ASSIRT Retiree Price Index

DOFA's understanding is that the ASSIRT Retiree Price Index is a measure of inflation based on the spending patterns of self-funded retirees, that is, they are based on the CPI but weighted to reflect assumed spending patterns of self-funded retirees aged 55 and over.

The cost of changing from CPI to this index would depend upon the difference between the Retiree Index and CPI. Information suggests that the difference has not been significant.