



Australian Defence Force Retirees Association Inc.

No. A0108026R

We represent the interests of Defence Force Retirees regarding their Superannuation

Meeting with

The Hon Matt Keogh MP

Minister for Veterans Affairs and Defence Personnel

6 September 2022

Presentation by: Herb Ellerbock

Secretary, ADFRA

Introduction

Minister, thank you for taking the time to listen to our concerns regarding the DFRDB scheme.

Those concerns have been expressed for a long time now. But they have not been heeded.

About ADFRA

ADFRA was formed because **no other** Ex Service Organization has sufficient knowledge of the **Defence Force Retirement and Death Benefits (DFRDB)** scheme to advocate on behalf of recipient members and their dependants.

Background

Unlike any other contemporary Commonwealth Public Service or Military superannuation scheme, **DFRDB** is an **unfunded** scheme.

Member **contributions are absorbed** directly into the **Consolidated Revenue Fund (CRF)**, where they are **not invested** and **earn no income**.

The DFRDB scheme **provides defined benefits** based **solely** on length of service and final salary.

100% of those benefits are **paid from the CRF**.

Background

The DFRDB scheme was introduced immediately after Australia's withdrawal from the Vietnam conflict, when **morale** and the **retention** of experienced personnel were at an **all-time low**.

The **DFRDB** scheme provisions were **used as an incentive** to **increase** member **retention**. But **members were given incorrect advice** about those provisions.

DFRDB recipients first **became aware** that the effect of **some provisions** in the DFRDB Act **diminished** their anticipated **benefits**, and those of their spouses, **in around 1997**.

Background

In 2014, after a lengthy campaign by the **Alliance of Defence Service Organizations (ADSO)** and individual superannuants, an amendment titled Defence Force Retirement Benefits Legislation Amendment (**Fair Indexation**) Act 2014 was incorporated in the DFRDB Act.

However, the **ADSO** campaign **was not aware** that a part of DFRDB benefits was excluded from indexation.

The **effect of Fair Indexation was not fair**. It **failed to restore benefits**, eroded by the Consumer Price Index, **to a fair current value**, and continued to **unfairly index** the benefits of **members aged under 55**.

Background

In 2019, there was an own motion **investigation by the Commonwealth Ombudsman**.

And **in 2021**, an **inquiry by the Senate Foreign Affairs, Defence and Trade Reference Committee**.

But the **Terms of Reference** for both those inquiries focused on what members were told about the scheme, **ensuring the effects of the legislation would not be considered**.

Presentation

The purpose of this presentation is to demonstrate:

- The **operation of Section 98B Increase in Certain Pensions.**
- The **operation of Section 24 Commutation of Retirement Pay,** which is replicated by Section 32A Commutation of Class C invalidity pay.
- And the **effect of the Schedule 3 Expectation of Life Factors and the Consumer Price Index.**

Partial Indexation of DFRDB Benefits

The **purpose** of Section 98B is **to maintain** the **relativity**, that is, the **purchasing power** of DFRDB benefits.

However, subsection 98B(5) **excludes a part** of DFRDB Benefits, determined by the Schedule 3 **Expectation of Life Factors*** **from** the application of **indexation** increases.

This exclusion is based on the indexation of the **funded** Commonwealth Superannuation Schemes and the **funded DFRB** scheme, the **predecessor** to the DFRDB scheme.

* From the Australian Bureau of Statistics **1960-1962** Life Tables

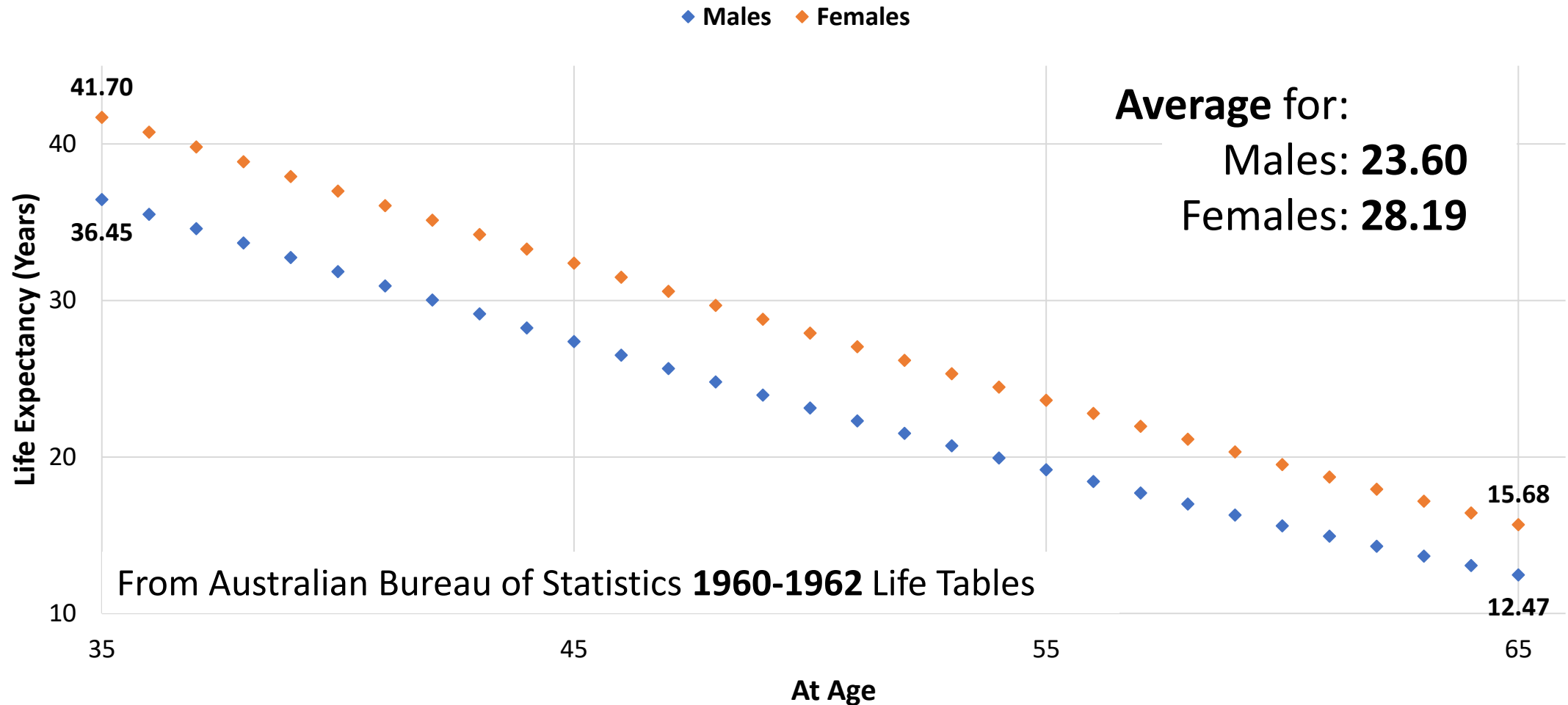
Partial Indexation of DFRDB Benefits

In the **funded** Commonwealth Superannuation Schemes, **five-sevenths** of benefits was paid from the **Consolidated Revenue Fund (CRF)** and **two-sevenths** was paid from a Fund comprising members' contributions and investment returns.

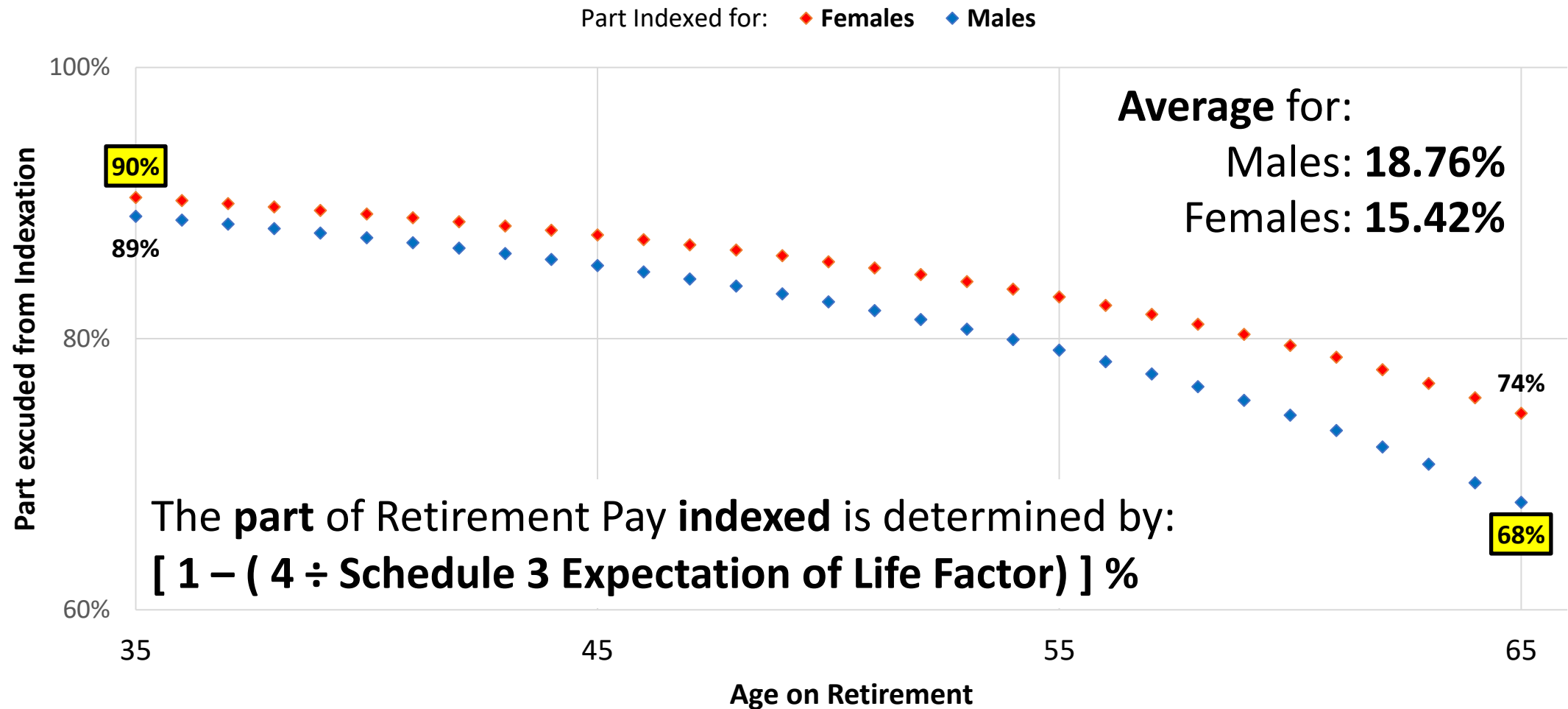
Only the portion paid from the **CRF** is indexed.

In the **unfunded** DFRDB scheme, member contributions are **not invested** and **earn no income**. **100%** of the **defined benefits** are **paid from the CRF**, but only **68% to 90%**, depending on members' gender and age, **is indexed**.

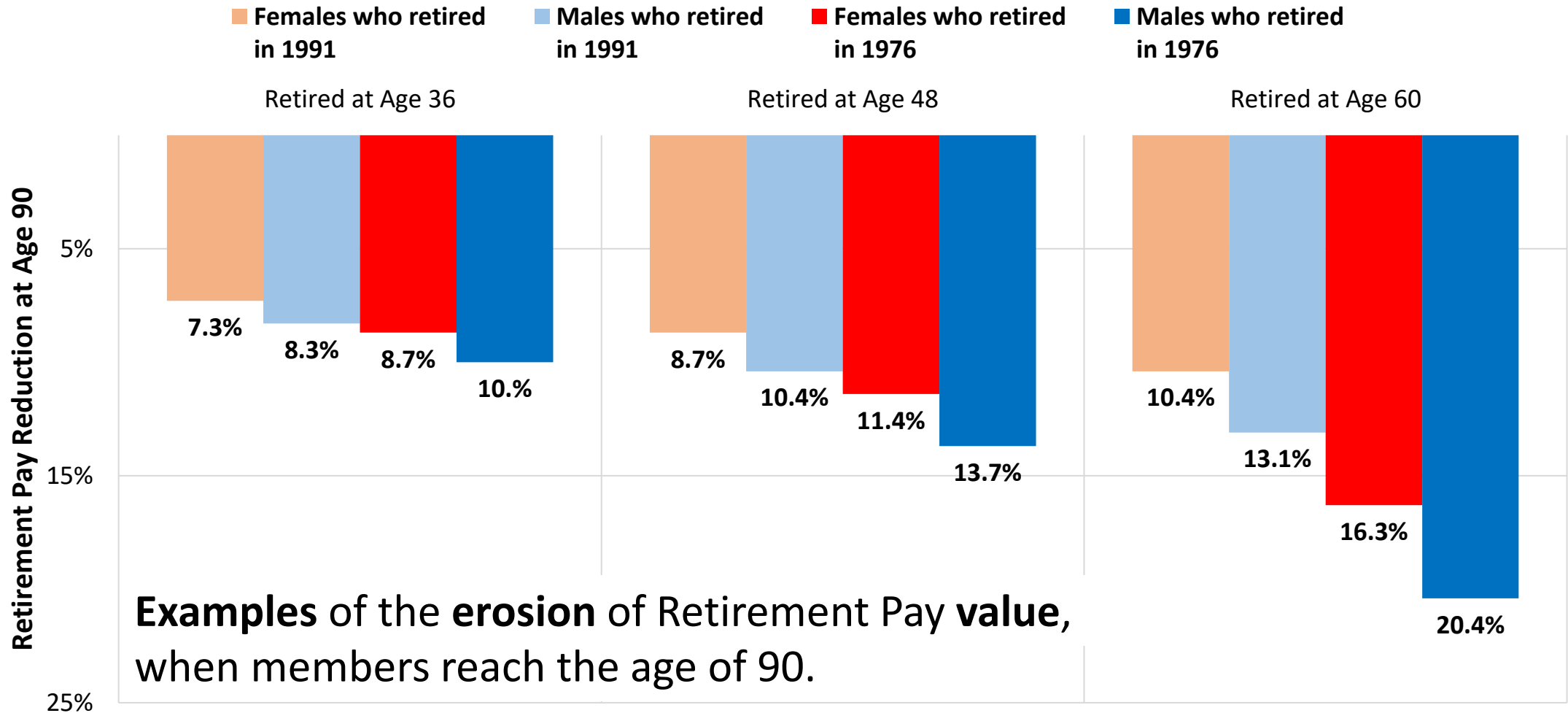
Schedule 3 Expectation of Life Factors



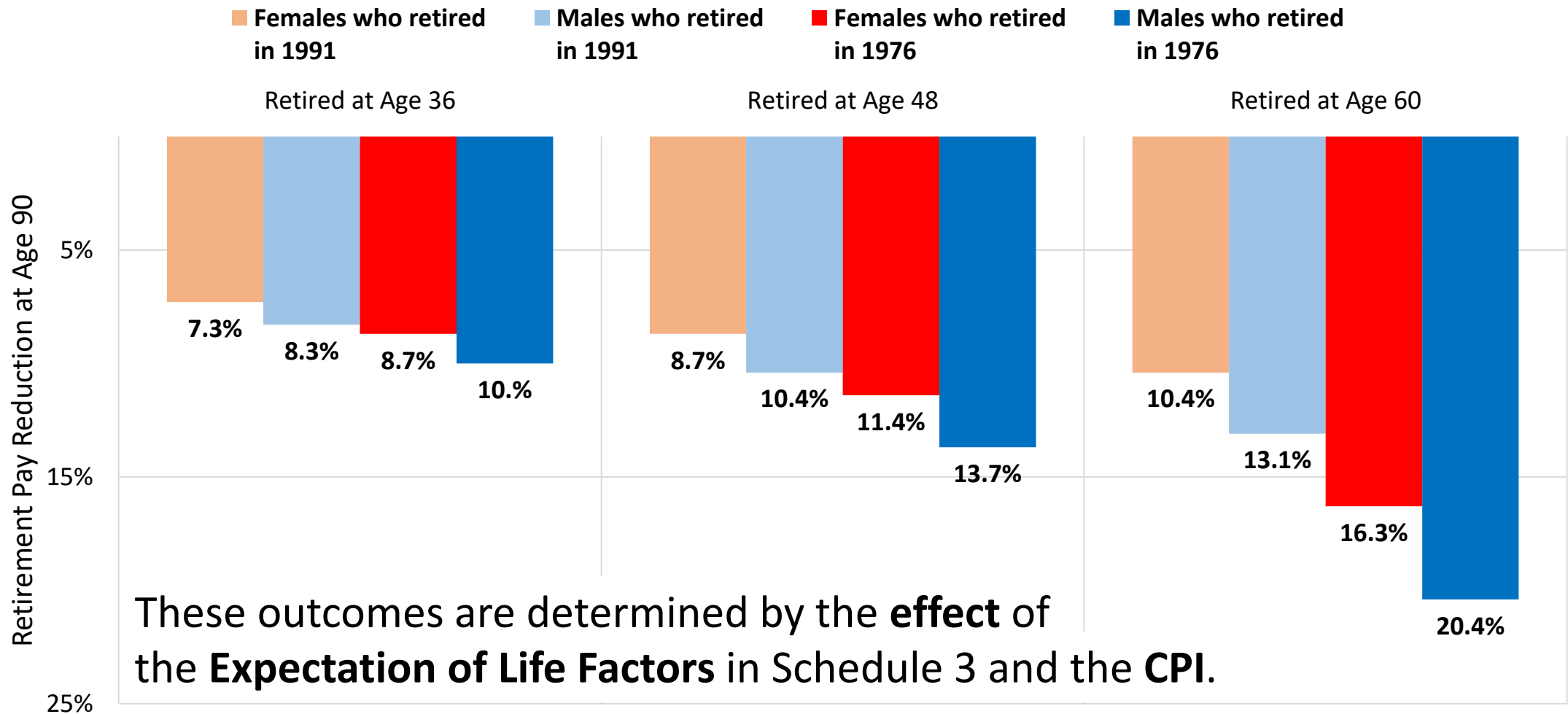
Part of DFRDB Benefits not indexed



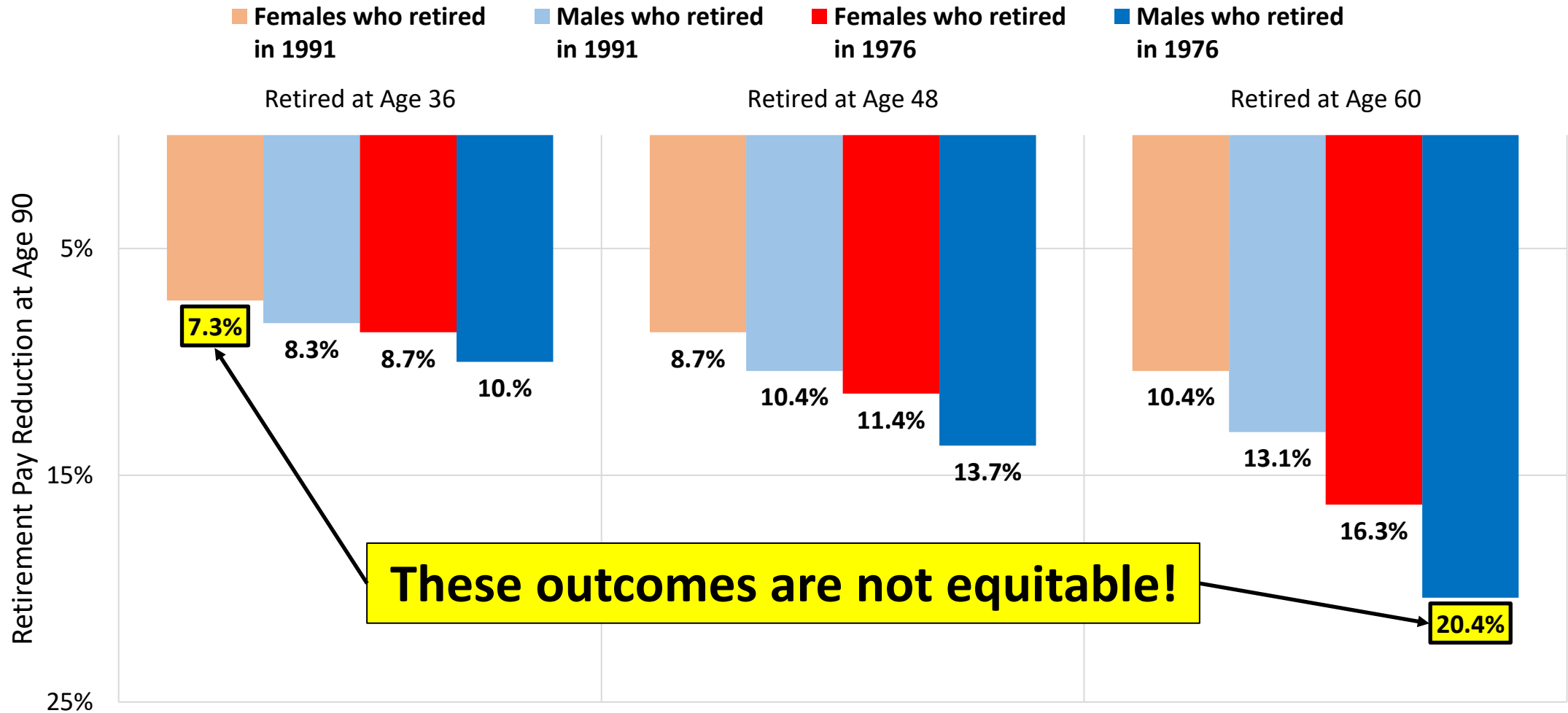
Inequitable Erosion of Benefits



Inequitable Erosion of Benefits



Inequitable Erosion of Benefits



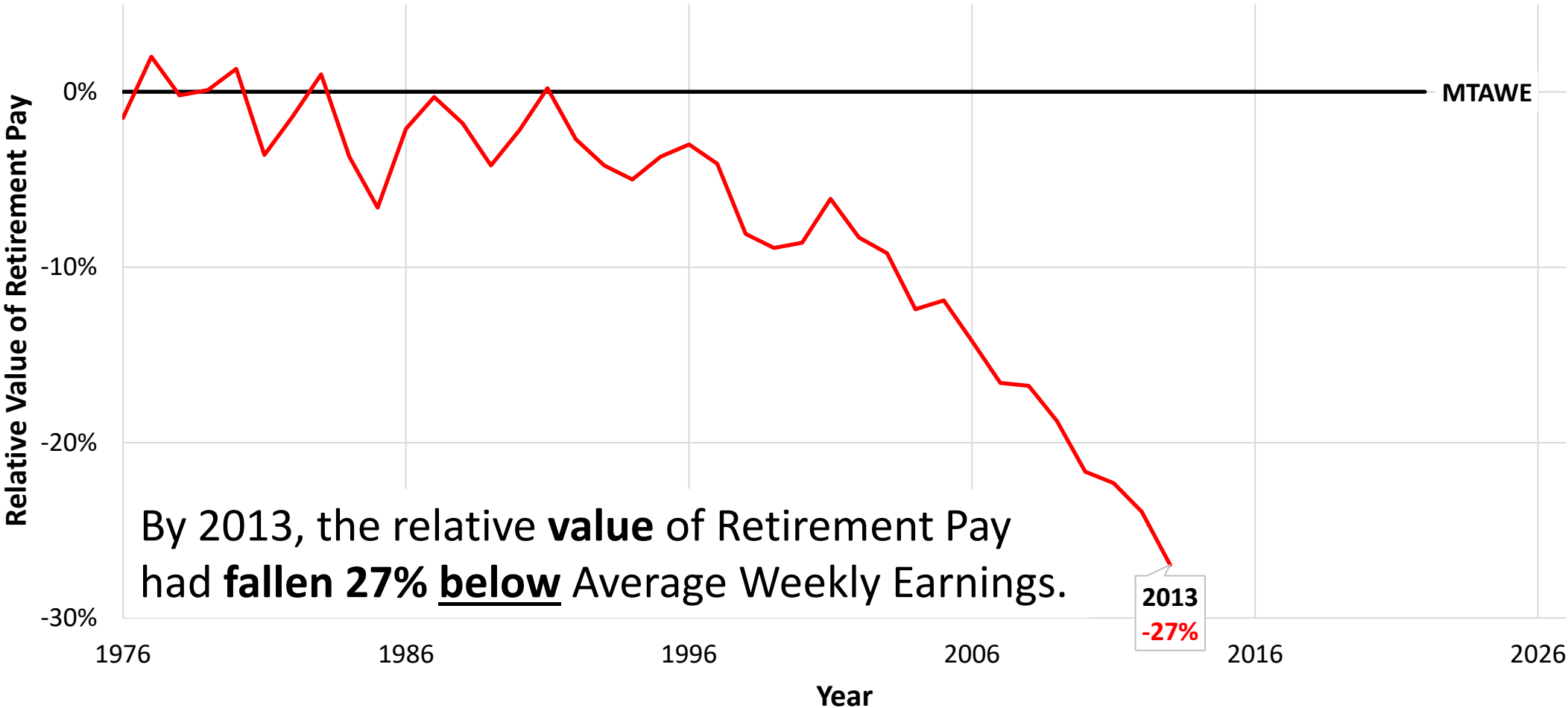
Effect of the Consumer Price Index

The **purpose of the Index** to which DFRDB adjustments are aligned, is **to maintain purchasing power** of DFRDB benefits.

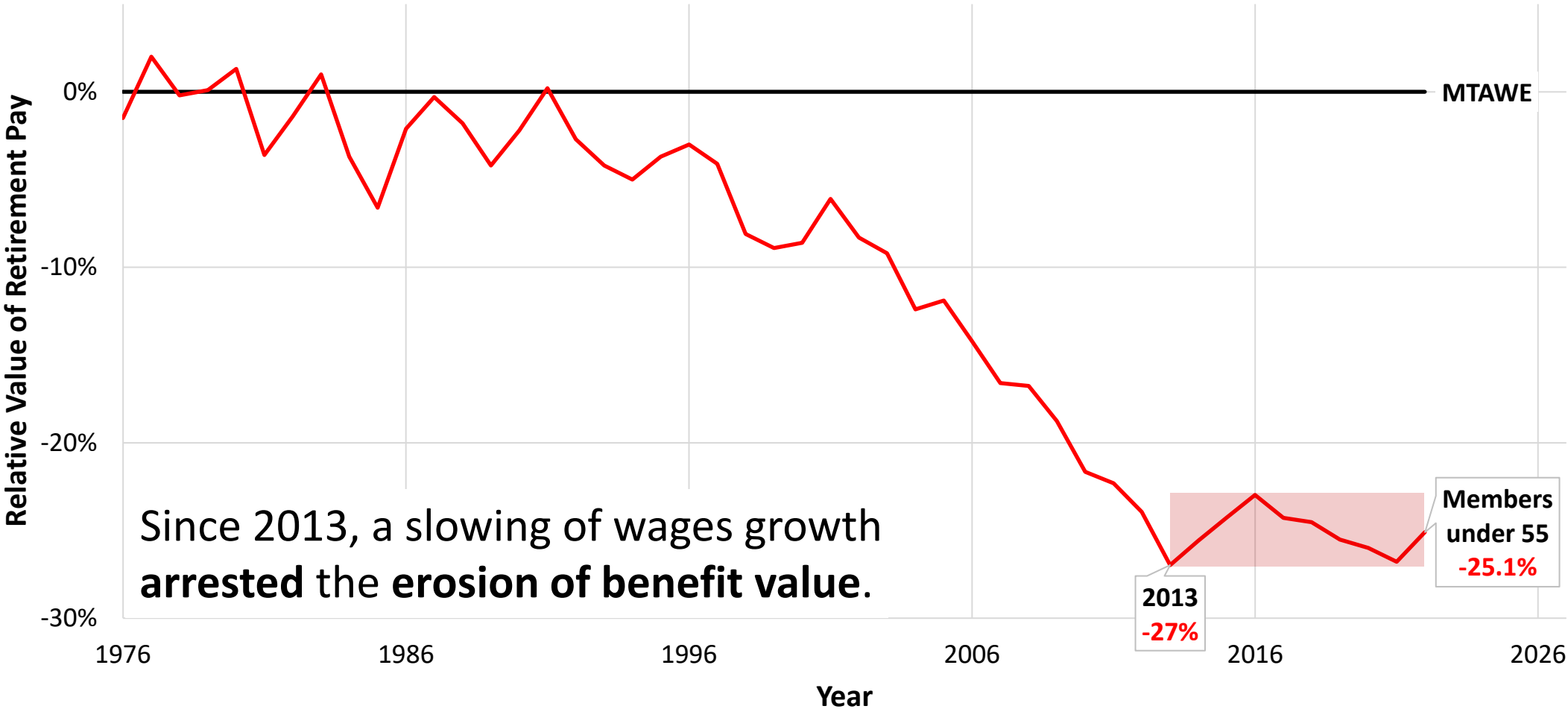
Effective **from 1 July 1976**, DFRDB benefit adjustments were **linked directly** to the **Consumer Price Index**, despite being **deemed** by the Joint Select Committee on Defence Forces Retirement Benefits Legislation, **in 1972**, to:

“Not fairly represent changes in general community standards”.

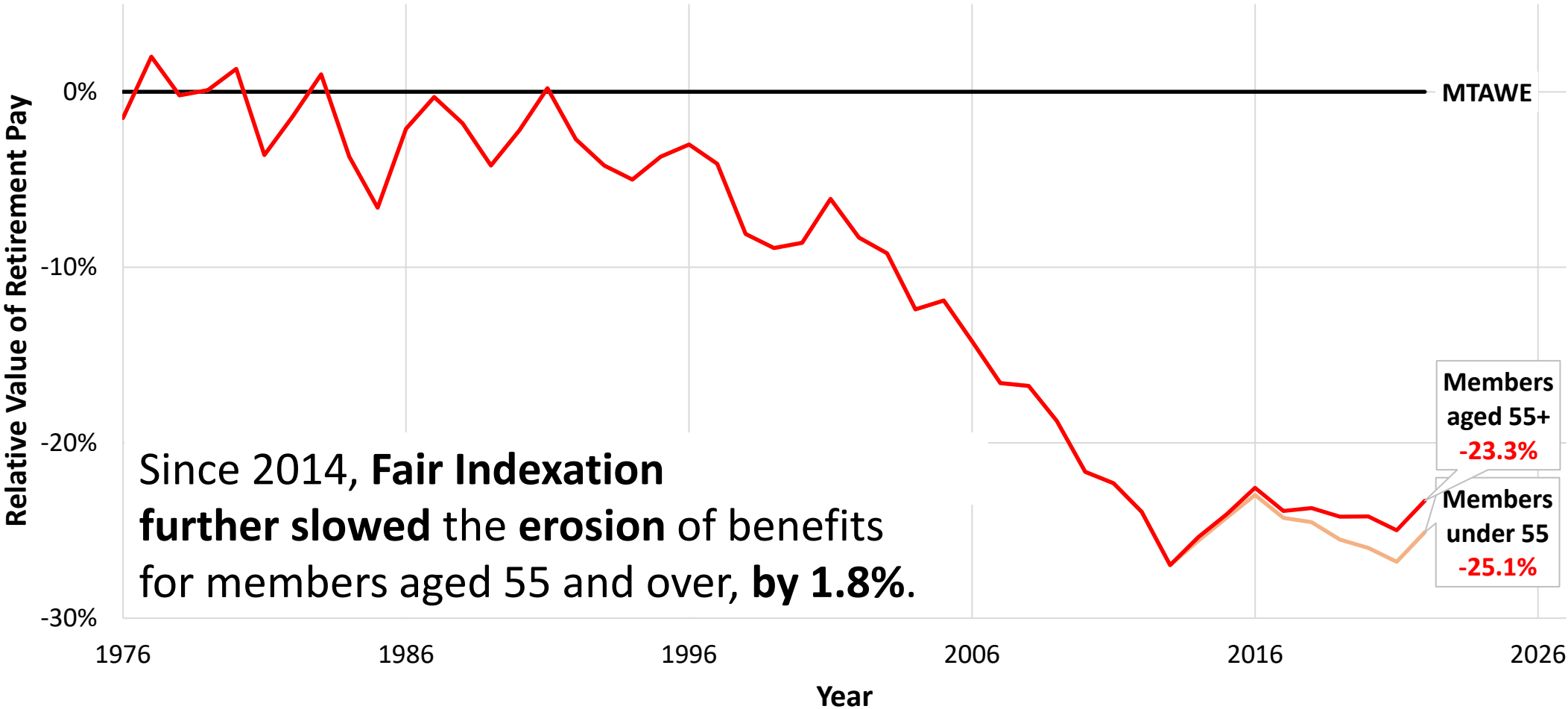
Effect of the Consumer Price Index



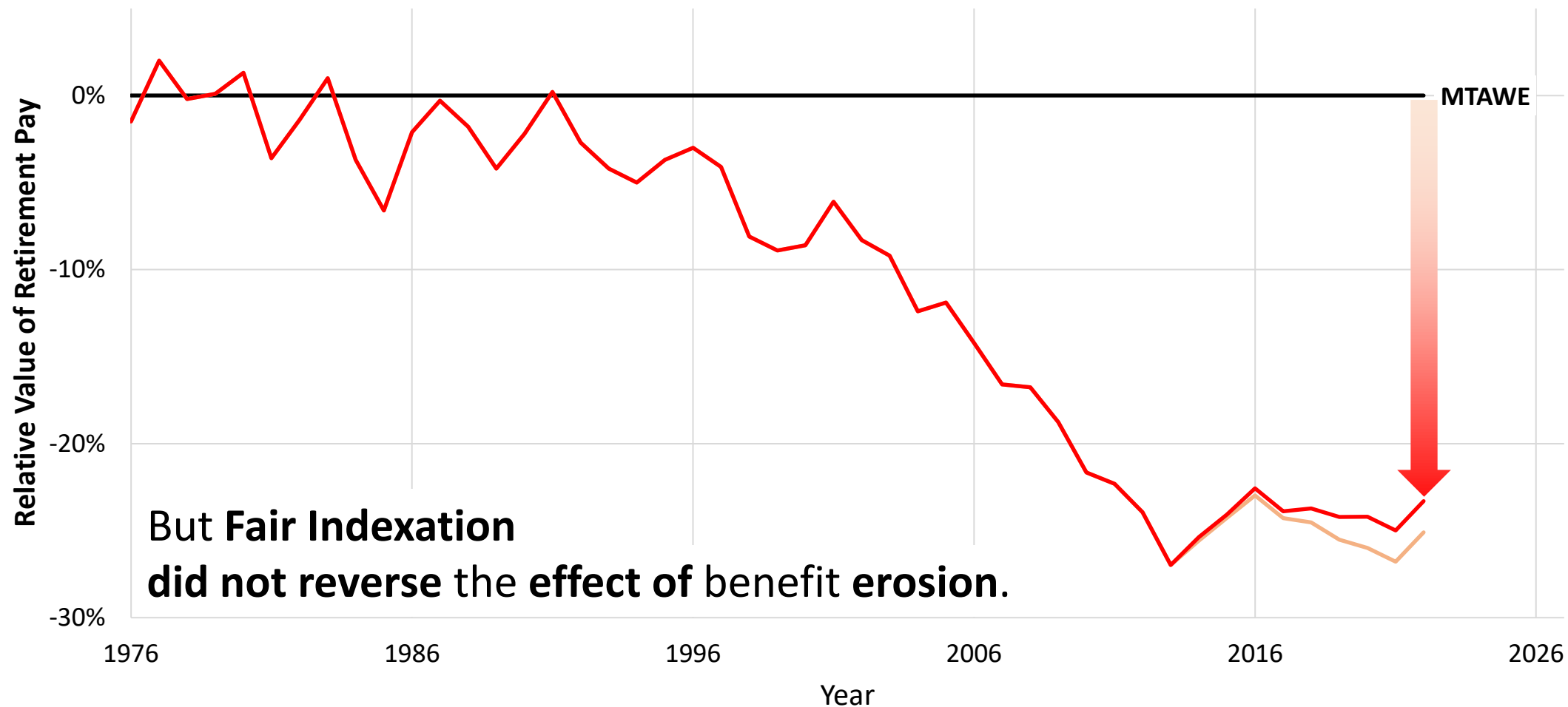
Effect of the Consumer Price Index



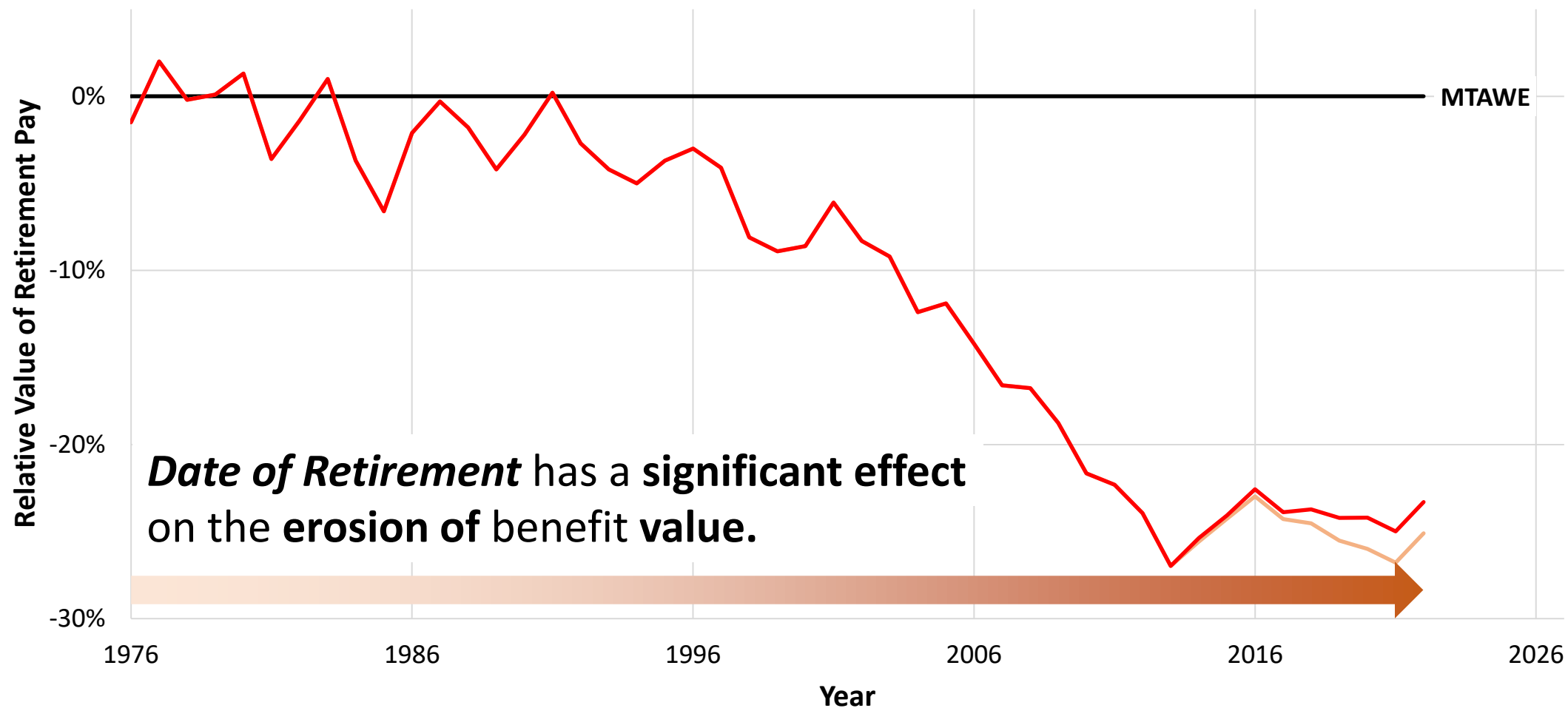
Effect of the Consumer Price Index



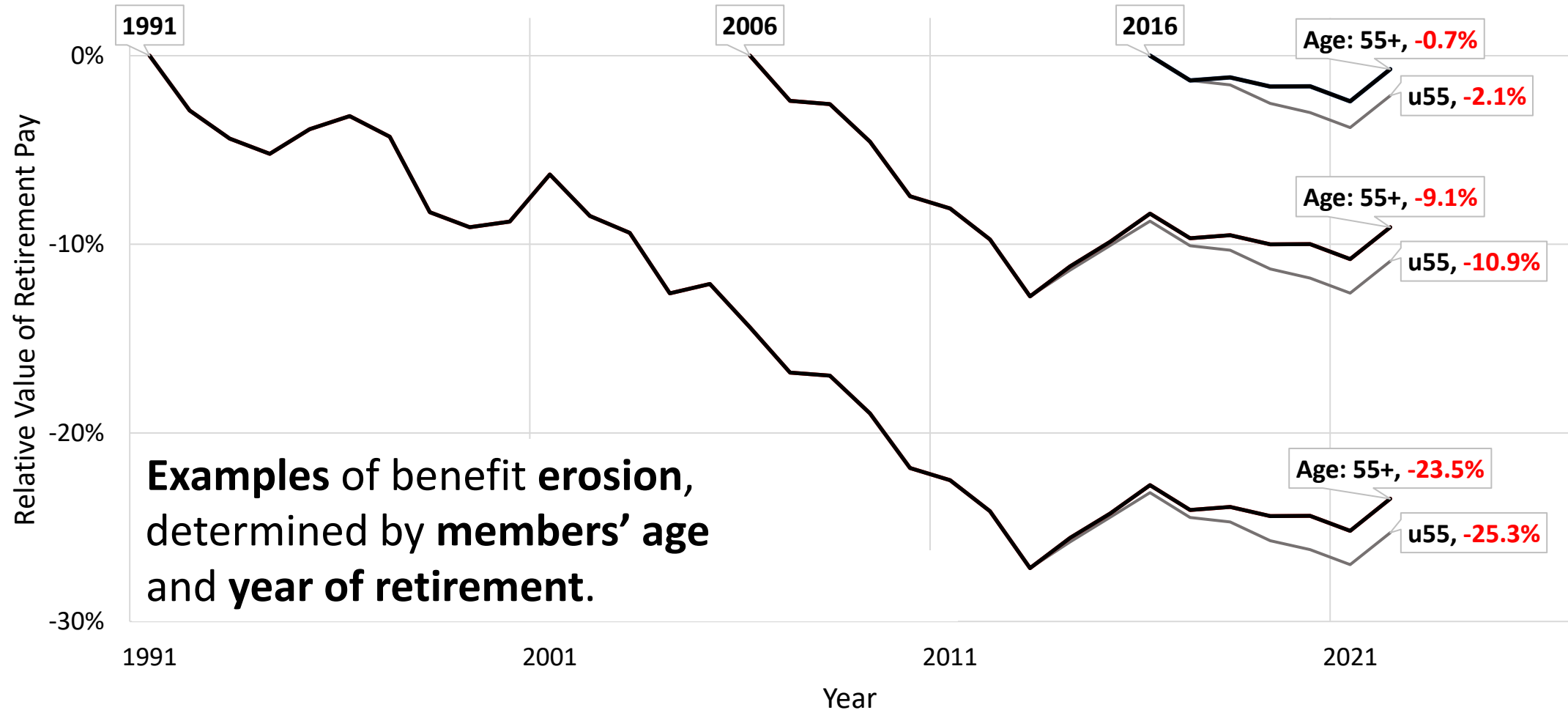
Effect of the Consumer Price Index



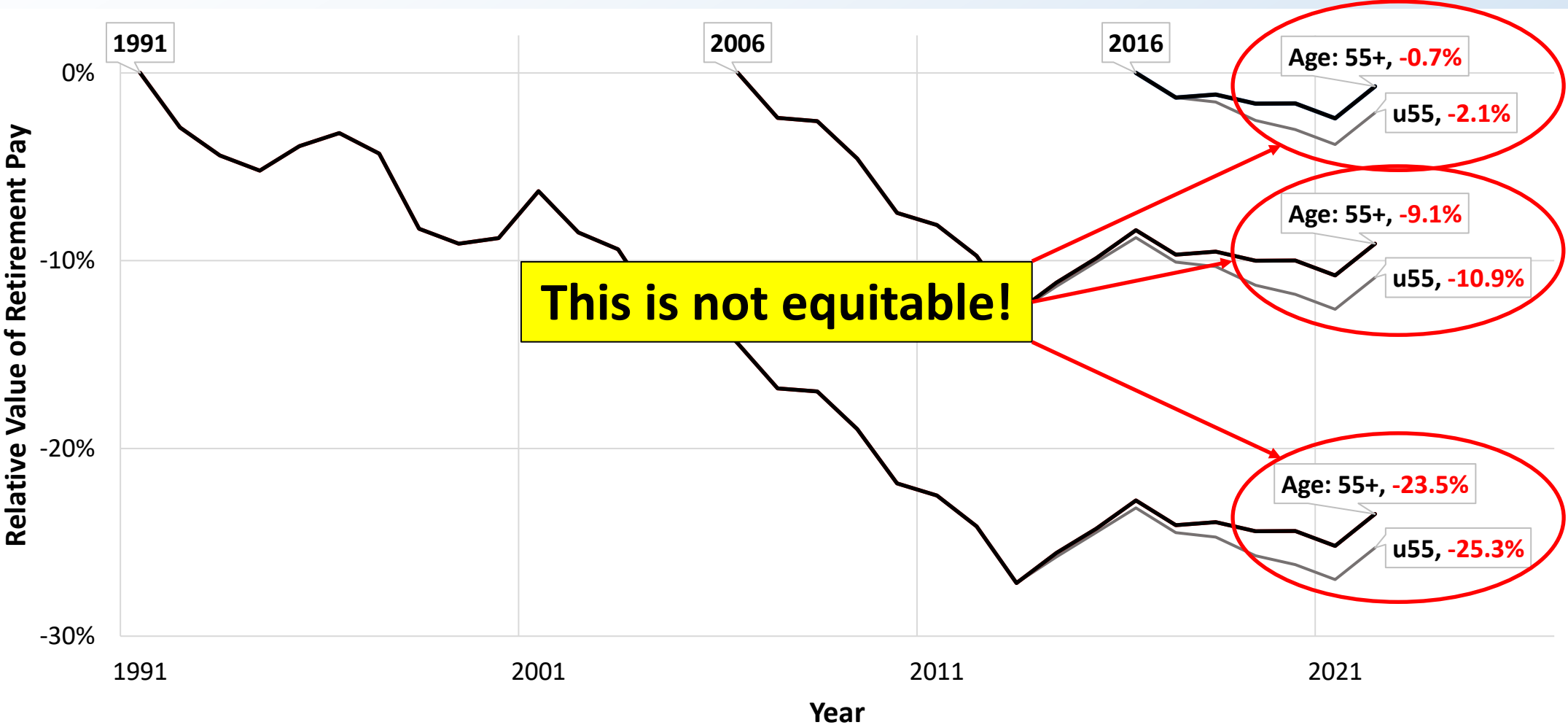
Effect of the Consumer Price Index



Effect of the Consumer Price Index



Effect of the Consumer Price Index



Effect on Spouses' Pensions

The **spouse** of a deceased recipient member is **entitled** to a **Spouse's Pension** at a rate equal to **five-eighths** of the member's **uncommuted** benefit.

Therefore, the **eroding effects** of the **Expectation of Life Factors** and **Consumer Price Index**, on recipient members' benefits, **apply equally** to *Spouses' Pensions*.

Resulting in the same inequitable outcomes!

Effect of Section 24

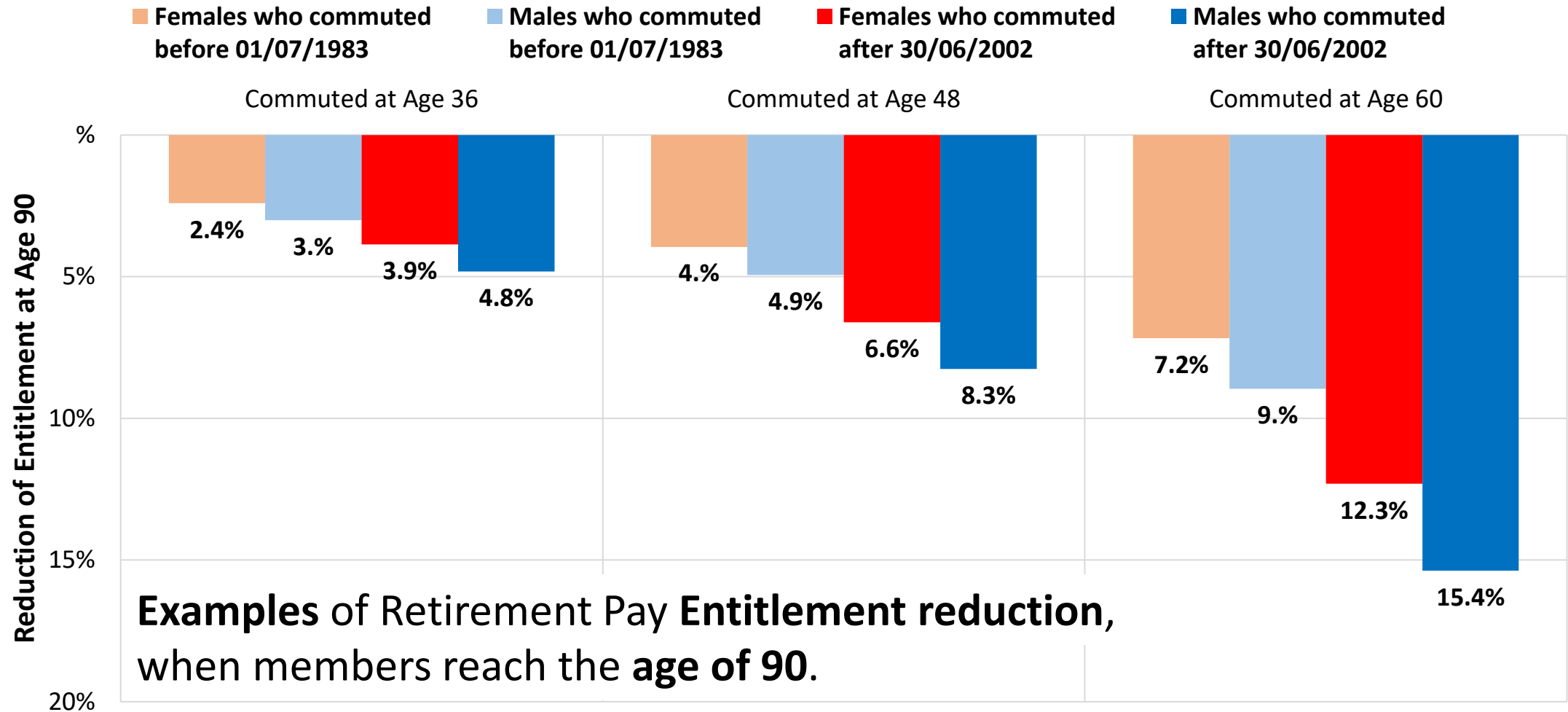
The **purpose** of Section 24 is to **provide a part pre-payment** of their Retirement Pay ***Entitlement***, to help members **resettle** into civilian life, **after** their **extended** period of **service**.

Subsection 24(3)(b) **proportionately** reduces members' Retirement Pay by an amount determined by the Schedule 3 **Expectation of Life Factors***. But it applies the reduction **permanently**.

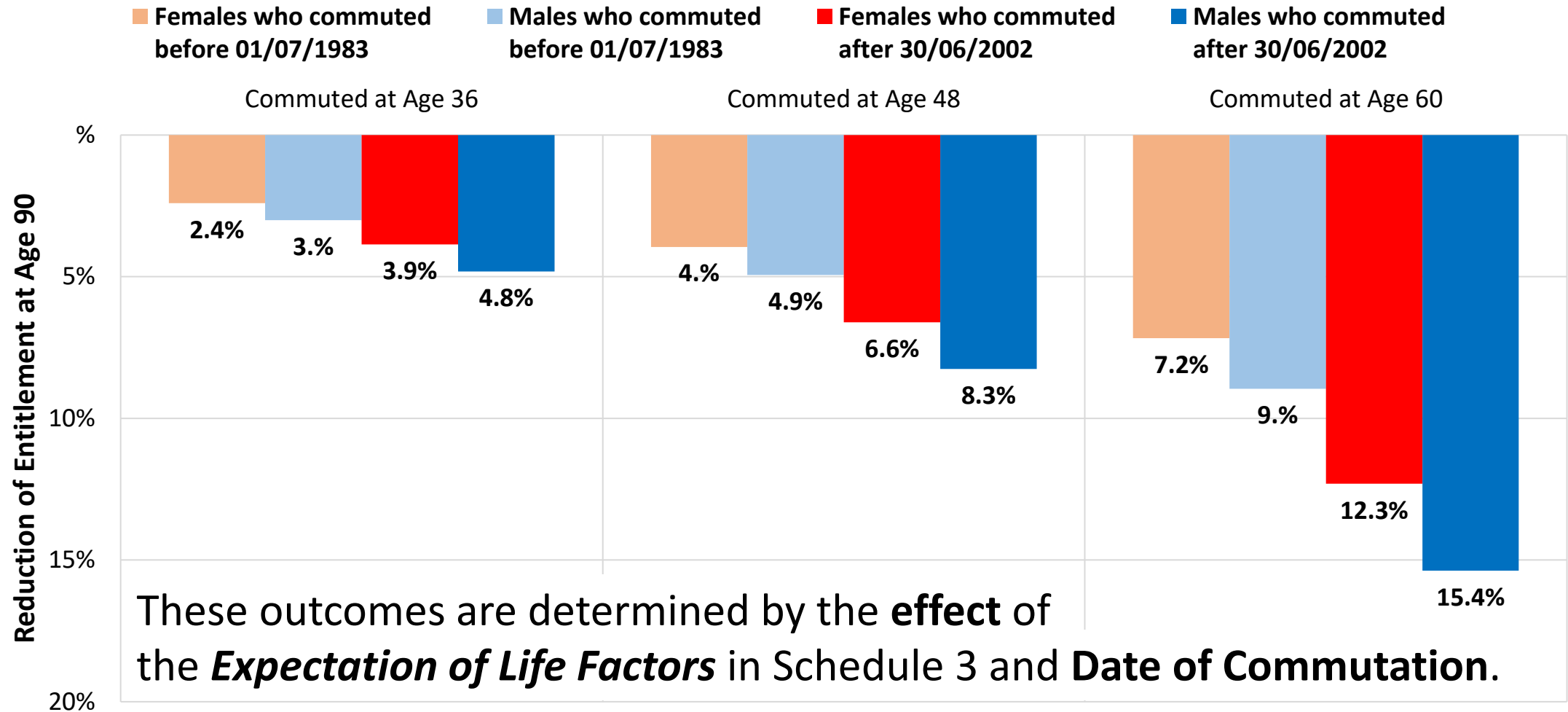
The **effect** is to **reduce** members' Retirement Pay **Entitlement**, if they live beyond their **notional (1960-1962)** Life Expectancy.

* From the Australian Bureau of Statistics **1960-1962** Life Tables

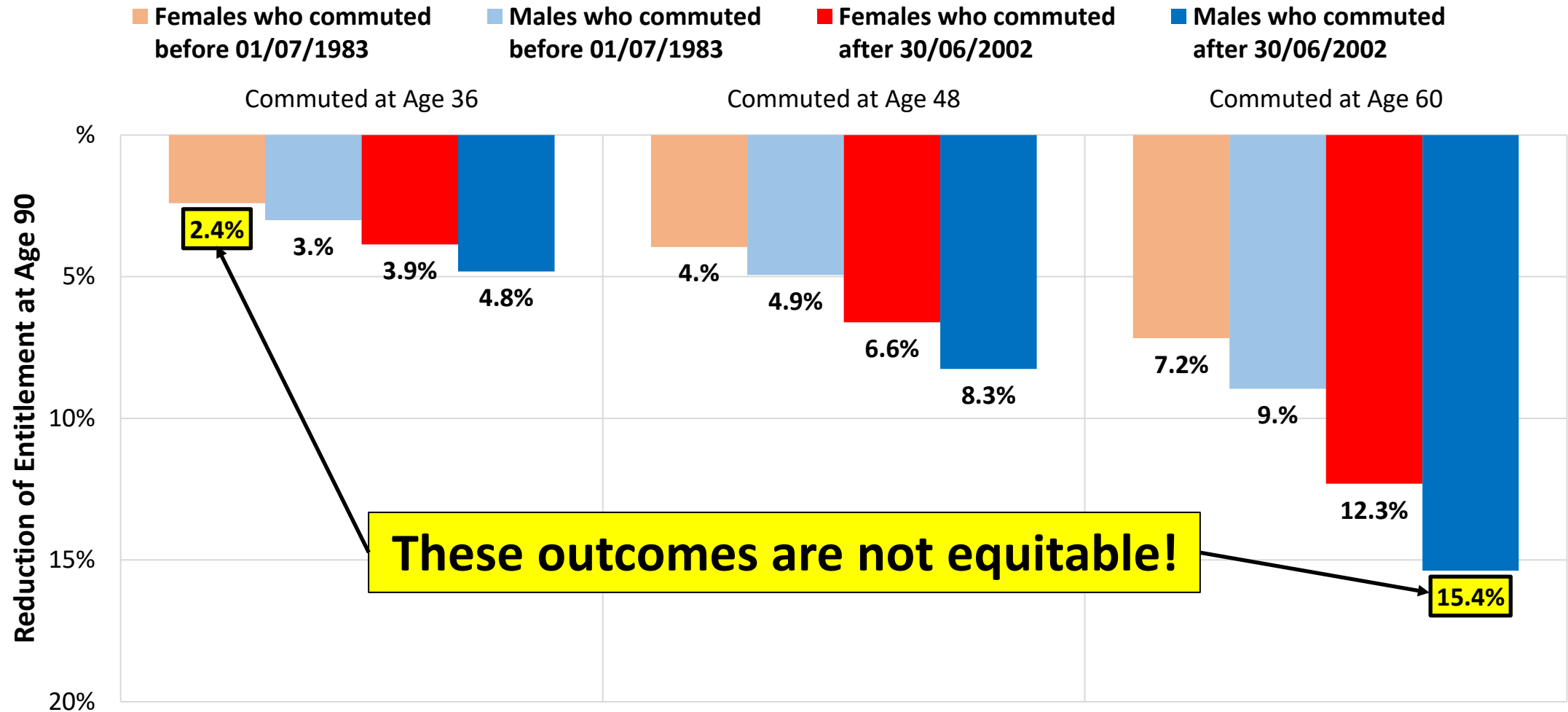
Effect of Section 24



Effect of Section 24



Effect of Section 24



Conclusion

Sections 98B and 24 produce **grossly inequitable outcomes** due to effects of:

- The Schedule 3 **Expectation of Life Factors**
- The **Consumer Price Index**.
- And the **Date of Retirement/Commutation**.

These effects are cumulative!

Effect of DFRDB on Age/Service Pensions

For every \$1 increase in DFRDB payments, Age/Service Pension payments are decreased by 50 cents.

DFRDB benefits and *Age/Service Pension* payments are indexed in the same manner.

However, the **income free area** for Age/Service Pension payments **is not adjusted in line with the Age/Service Pension payments.**

That introduces **income creep** which reduces the rate of **Age/Service Pension** payments and results in a **net reduction of combined DFRDB and Age/Service Pension payments.**

Conclusion

Even though Australian Historical Population Statistics showed that **Life Expectancy increased** over time, the implementation of **Commutation** in the DFRDB scheme **made no provision** for it.

Because the Schedule 3 **Expectation of Life Factors** remain static, they **do not represent** actual Life Expectancy.

Even though the **Consumer Price Index (CPI)** had already been deemed **unsuitable**, the **Indexation** of DFRDB benefits **made no provision** for the eventuality that the **CPI** would not maintain the relativity/purchasing power of those benefits.

Conclusion

Given that the Schedule 3 **Expectation of Life Factors** and the **Consumer Price Index** becoming **unrepresentative** was not anticipated, it is reasonable to ask:

- Are the detrimental and **inequitable effects** of *Section 98B* and Section 24 **intended outcomes**?
- Do those outcomes constitute **fair and reasonable treatment** of the men and women who **dedicated a substantial part of their lives to the service of their country** in the Australian Defence Force?

Conclusion

A **significant factor** in most members' decision to continue serving in the Defence Forces for more than 20 years, was the **anticipation** of a **fully indexed** retirement benefit.

But the **operation** of the **Indexation** and **Commutation** provisions in the legislation, and **effect** of the **Expectation of Life Factors** and the **Consumer Price Index**,

ensure that **expectation** will never be fulfilled.

Remediation Sought

DFRDB recipients are **seeking**:

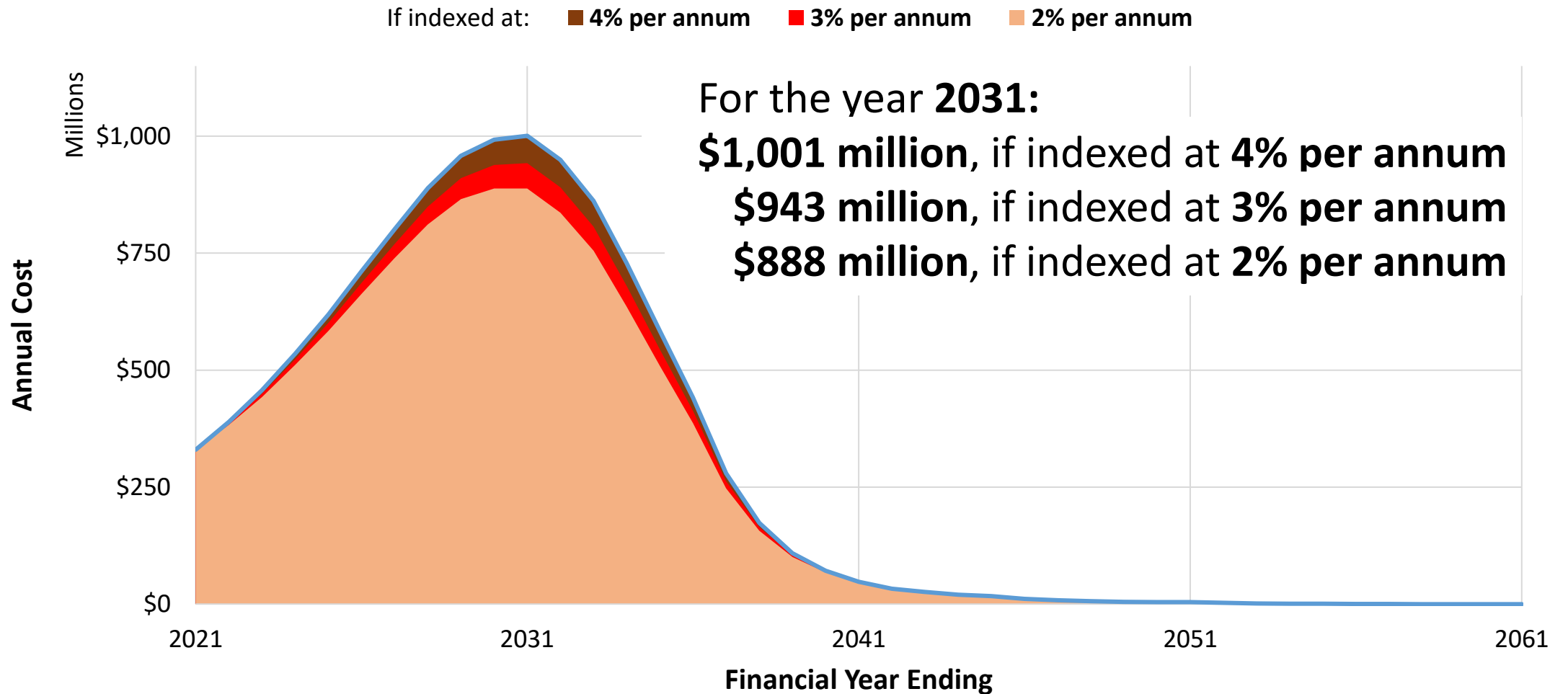
- A **review** of the DFRDB Act and the **removal** of the **benefit erosion provisions**;
- The **restoration** of benefits to a **fair, current value**; and
- The **reimbursement** of Entitlement **reductions which exceed the amount commuted**.

Cost of Remediation

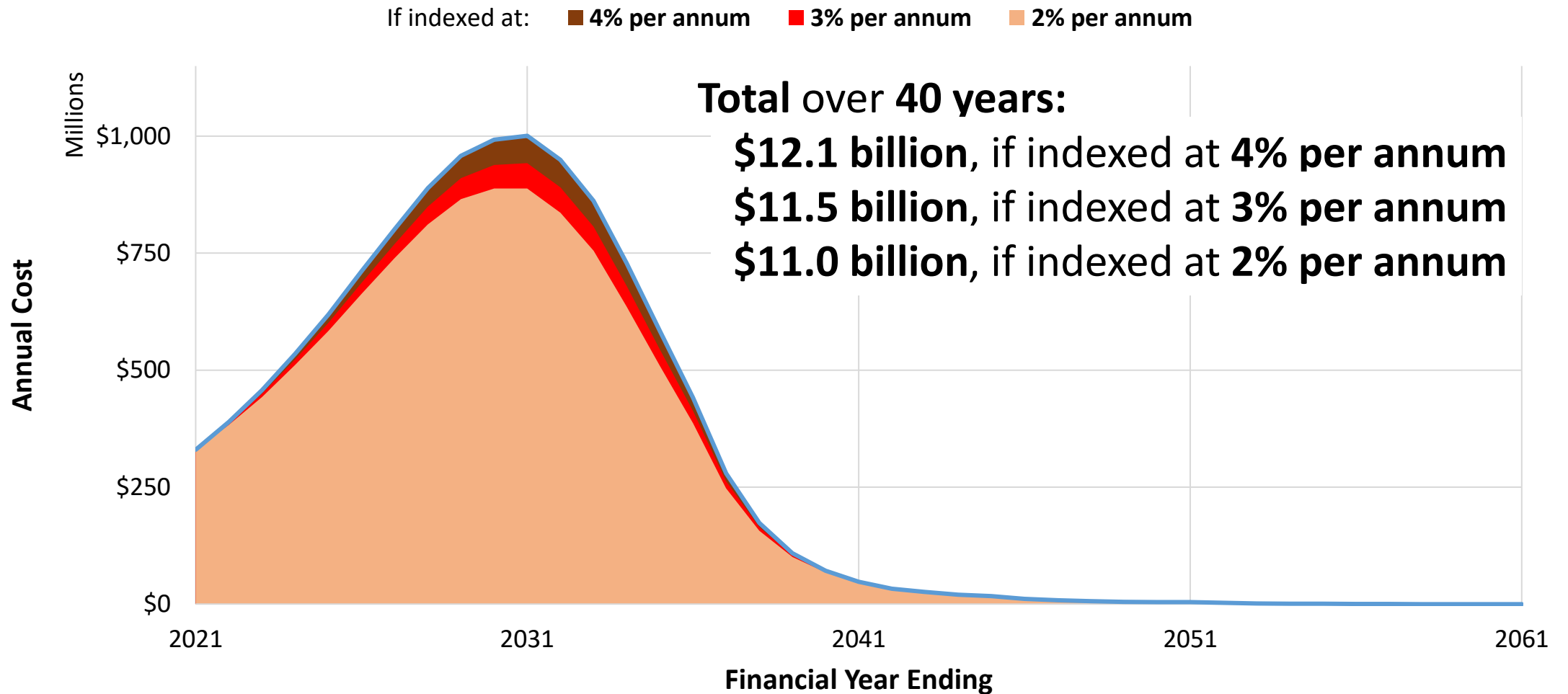
Commonwealth Superannuation Corporation has **denied all requests** for the recipient member data required to determine the cost of remediation.

However, based on a **650-member sample** population of recipients, an indicative **estimate** of the **cost** of remediation **over the next 40 years** has been determined.

Cost of Remediation



Cost of Remediation



Remediation Funding

The **anticipated** response from Government is:

Even if the Government was willing, in the current economic climate, **the Budget could not afford these remedies.**

However,

the **cost of remediation** should be **funded by the Future Fund.**

Remediation Funding

According to Commonwealth Superannuation Corporation's Rules for Defined Benefits Funds:

“The **Future Fund** was established in 2006 to strengthen the Australian Government's long-term financial position and ensure that **from 2020, funds can be withdrawn** from it to cover the annual **unfunded** Commonwealth superannuation **liabilities** due to our ageing population.”

Remediation Funding

The **Future Fund** does **not** exist **just for** the **funded** Commonwealth Superannuation Scheme and the Public Sector Superannuation Scheme, or the Parliamentary Contributory Superannuation Scheme for pre-October 2004 Members of Parliament.

It also exists for the DFRDB scheme, which is **also** an **unfunded** Commonwealth Superannuation liability.

Remediation Funding

According to the **2020-2021 Annual Report**, the **Future Fund** has grown to **\$196.8 billion** after delivering **22.2% growth** for the year.

Just a small part of that growth **would restore fairness and equity** for DFRDB scheme beneficiaries.

Minister, we look forward to your reply.