



Australian Government

**Defence Force Retirement &
Death Benefits Scheme**

Inquiry into the:

- **Governance of Australian Government Superannuation Schemes Bill 2010**
- **ComSuper Bill 2010**
- **Superannuation Legislation (Consequential Amendments and Transitional Provisions) Bill 2010**

Submission to the Senate Standing Committee on Finance and Public Administration (Legislation Committee)

March 2010

Summary

1. The Defence Force Retirement and Death Benefits (DFRDB) Authority accepts the assurances of the Australian Government that the interests of military scheme members will be appropriately represented by the new Trustee entity, the Commonwealth Superannuation Corporation (CSC), to be established by Governance of Australian Government Superannuation Schemes Bill 2010. Therefore it is the view of the DFRDB Authority that it is not necessary to retain a separate board to administer the military superannuation schemes.
2. The DFRDB Authority notes that the proposed membership of the CSC includes two members (out of ten) nominated by the Chief of the Defence Force. The Explanatory Memorandum to the Governance of Australian Government Superannuation Scheme Bill 2010 also notes the intention that the Finance Minister would consult with Ministers in the Defence Portfolio in selecting the five “*employer directors*”¹.
3. The changed arrangements also provide that the CSC may establish a Defence Force Case Assessment Committee (DFCAC) to review decisions referred to by the CSC. The DFCAC, if established, will include three members nominated by the Chiefs of the three Services (similar to the current membership of the DFRDB Authority).
4. The DFRDB Authority considers that there are four significant differences between the DFRB/DFRDB and the civilian defined benefits schemes:
 - a. Rate of Member contributions and absence of investment fund;
 - b. Ability to join another Commonwealth Government scheme in order to make ancillary contributions;
 - c. Re-entry to the ADF and the DFRDB;
 - d. Access to benefits after 20 years service; and
 - e. Relative complexity of invalidity retirement benefits.

¹ The remaining three directors being nominated by the Australian Council of Trade Unions.

5. The DFRDB Authority notes that under the current arrangements its Chair is also the Commissioner for Superannuation and the CEO of ComSuper (the provider of administration services). The DFRDB Authority considers that the Commissioner discharges this dual responsibility without favour to the DFRDB Authority or detriment to any of the other civilian and military schemes administered by ComSuper. The removal of this dual role through the proposed establishment of ComSuper as a statutory agency, separate to the CSC, is considered unlikely to have a material impact on the DFRB/DFRDB members and in fact would remove the need manage this potential conflict.
6. The DFRDB Authority also notes that the CSC may appoint its own staff to provide administrative and secretariat support. The DFRDB Authority currently relies on administrative support provided by the Commissioner for Superannuation and staff of ComSuper. In undertaking its functions in relation to the DFRB and DFRDB schemes in future, the CSC will not be reliant on such external support.
7. The DFRDB Authority notes that key benefits anticipated by the Australian Government in relation to the Governance of Australian Government Superannuation Scheme Bill 2010 are:
 - a. Consolidation will enable a single trustee to deal with a single provider of administration services for all of the military and civilian defined benefits schemes; and
 - b. Consolidation will enable a single trustee to achieve cost reductions in managing the invested funds of members.
8. While not disagreeing with the any element of the proposals, the DFRDB Authority notes in relation to the anticipated benefits that under the current legislative framework DFRB/DFRDB members' administration services are already provided by a single service provider. The DFRDB Authority also notes that on 26 November 2009, the Minister for Finance and Deregulation announced that the Australian Government will, from 1 July 2012, "*outsource the administration services of PSSap*". This means that the CSC will in due course need to engage and oversee a second administration service provider (in addition to ComSuper which will continue to administer the military and civilian defined benefits schemes) which has the potential to impact the resources available to oversee the DFRB and DFRDB schemes.

9. The DFRDB Authority also notes that the contributions of DFRDB members are directed to the Consolidated Revenue Fund (CRF). There is no DFRDB investment fund so there are no DFRDB related economies to be achieved in consolidating investment management costs.

10. The DFRDB Authority notes that subclause 35(2) of the Governance and Australian Government Superannuation Schemes Bill 2010 which refers to the DFCAC may be confusing. It refers to decisions made under both the *Defence Forces Retirement Benefits Act 1948* (the DFRB Act) and the *Defence Force Retirement and Death Benefits Act 1973* (the DFRDB Act). Subsequent references to the establishment of the DFCAC in Column 1 then refer to the DFCAC established under “section 100 of that Act”. It is understood that the new section 100 establishing the DFCAC is to be inserted only into the DFRDB Act.

Background

1. The DFRDB Authority welcomes the opportunity to provide comments to the Senate Standing Committee on Public Administration - Legislation Committee (the Committee) regarding the following Bills:
 - a. Governance of Australian Government Superannuation Schemes Bill 2010;
 - b. ComSuper Bill 2010; and
 - c. Superannuation Legislation (Consequential Amendments and Transitional Provisions) Bill 2010.
2. The DFRDB Authority notes that the Committee has been asked to determine:
 - a. whether it is necessary to retain a separate board to administer the military superannuation schemes; and
 - b. whether these schemes differ markedly from other Commonwealth Government administered schemes.
3. The DFRDB Authority submission is in relation to these questions as they apply to the DFRB and DFRDB schemes only.

The DFRDB Authority

4. The DFRDB Authority is established by section 8 of the *Defence Force Retirement and Death Benefits Act 1973* (the DFRDB Act). Under paragraph 8(2)(a) of the DFRDB Act, the Commissioner for Superannuation is *ex-officio* Chairman of the Authority. There are four other Authority members, all of whom are appointed by the Minister for Defence Personnel, Materiel and Science. These other members are appointed for two years and may be reappointed at the end of their term.
5. The DFRDB Authority, with administrative support provided by the Commissioner for Superannuation and staff of ComSuper², acts as Trustee for the DFRB and DFRDB schemes. The Authority delegates most of its powers to ComSuper staff for the purpose of day-to-day scheme administration. The Authority retains the power to reconsider decisions made by delegates.

² ComSuper is comprised of the staff that assist the Commissioner in carrying out his or her functions. ComSuper is a prescribed agency the *Financial Management and Accountability Act 1997*.

6. The DFRDB Authority also monitors the implementation of the schemes' rules by ComSuper for any individual or systemic issues. The DFRDB Authority also undertakes reconsiderations of initial decisions of its delegates.
7. The DFRDB Authority acknowledges that the effect of the Bills is to merge the DRRDB Authority with a new Trustee entity, the Commonwealth Superannuation Corporation (CSC) which will then assume responsibility for managing the DFRB and DFRDB Schemes.

The DFRB and DFRDB schemes

8. The DFRDB scheme is a fully unfunded defined benefits scheme established under the DFRDB Act. The DFRB scheme is established under the *Defence Forces Retirement Benefits Act 1948* (the DFRB Act).
9. The DFRDB Scheme provides benefits for members who entered the Australian Defence Force (ADF) between 1 October 1972 and 30 September 1991³, and also for contributors to the DFRB Scheme who were compulsorily transferred to the DFRDB Scheme from its inception in 1972. It is only those DFRB members who were in receipt of benefits/pensions in 1972 that continue to be administered under the DFRB Act i.e. there are no remaining contributory members of the DFRB scheme. For this reason the majority of the references that follow are to the DFRDB only.
10. With the commencement of the Military Superannuation and Benefits Scheme (MSB scheme) on 1 October 1991, the DFRDB Scheme was closed to all new ADF entrants. The existing members of the DFRDB Scheme were given the choice to remain in the Scheme or to transfer to the new MSB scheme⁴.
11. The DFRDB Scheme is a fully unfunded defined benefit superannuation scheme. Member contributions are received by ComSuper and transferred to the Australian Government's Consolidated Revenue Fund (CRF). There is no investment fund for the DFRDB Scheme and all benefits are paid from the CRF.

³ The DFRDB scheme was closed to new entrants on 1 July 1991. Since that time new entrants have been members of the MSB scheme.

⁴ The trustee of the MSB scheme is the Military Superannuation and benefits Board of Trustees No. 1 (the MSB Board)

12. The DFRDB scheme is an Exempt Public Sector Superannuation Scheme for the purposes of the *Superannuation Industry (Supervision) Act 1993* (the SIS Act), and is therefore deemed to be a complying superannuation fund under the *Income Tax Assessment Act 1997* and the *Superannuation Guarantee (Administration) Act 1992*. Although the DFRDB Authority endeavours to comply with the spirit of the SIS Act, it has not been necessary for it to elect that the Schemes become a Regulated Superannuation Fund subject to the prudential requirements in the SIS Act.

Is it necessary to retain a separate board to administer the military superannuation schemes?

Application of the schemes' rules

13. The DFRDB Act currently requires that the five member DFRDB Authority include three members – one each nominated by the Chiefs of the three Services; the Navy, Army and Air Force. In practice, the Service nominees are serving members of the ADF.
14. The DFRB and DFRDB Acts make up the scheme rules that are managed by the DFRDB Authority. There is anecdotal evidence that having ADF members make up the majority of the DFRDB Authority may provide some confidence to scheme members that the unique nature of their employment is taken into account in decision making. In practice the scheme rules themselves are intended to provide for this uniqueness.
15. For example, the ADF has the right to retire members on the grounds of invalidity if they do not meet strict medical standards - even though they may be capable of civilian employment of a similar nature. The scheme rules provide for a scaled system of invalidity classification with correspondingly scaled benefits. Decisions on the invalidity classification (and level of pension) of a member retired on medical grounds are generally made by (civilian) DFRDB Authority delegates in ComSuper.

Reconsideration of decisions

16. If a member seeks a reconsideration of a decision of the DFRDB Authority or its delegates, the case is currently referred to the full DFRDB Authority⁵. If a member remains dissatisfied with the decision as a result of that reconsideration, the member may seek a review by the Administrative Appeals Tribunal.
17. In the invalidity benefits example referred to above, during 2008-09, there were 48 initial DFRDB invalidity classifications made by civilian delegates of the DFRDB Authority (staff of ComSuper). On reconsideration, the DFRDB Authority varied classifications (not always to the benefit of members) on only 4 occasions in 2008-09. The most common reason for a varied decision being the presentation of new evidence not made available to the delegate in the initial decision.
18. In general, it can be said that the schemes' rules are sufficiently clear that decisions of civilian delegates are not materially different to decisions made by the DFRDB Authority with its majority of Service members.
19. The DFRDB Authority notes that the Superannuation Legislation (Consequential and Transitional Provisions) Bill 2010 provides that the CSC may establish a Defence Force Case Assessment Committee (DFCAC) to review decisions referred to it. The DFCAC, if established, will include three members nominated by the Chiefs of the three Services (similar to the current membership of the DFRDB Authority). This provides the CSC with a capacity to strengthen the input of Service personnel to decision making.
20. The DFRDB Authority notes that subclause 35(2) of the Governance and Australian Government Superannuation Schemes Bill 2010, which refers to the DFCAC, may be confusing. Column 1 of the relevant Table refers to decisions made under both the *Defence Forces Retirement Benefits Act 1948* (the DFRB Act) and the *Defence Force Retirement and Death Benefits Act 1973* (the DFRDB Act).

⁵ Note for the sake of completeness that Administrative Appeals Tribunal may review of decisions made by the DFRDB Authority.

21. Subsequent references to the establishment of the DFCAC in Column 2 of the Table then refer to the DFCAC established under “*section 100 of that Act*”. It is understood that the new section 100 establishing the DFCAC is to be inserted only into the DFRDB Act. This provision should be clarified.

Complaints

22. The largest number of complaints received by the DFRDB Authority, other than administration issues such as timeliness of payments and advice, relate to members who had rejoined the ADF but had not met the requirements for re-entry to the DFRDB. These members were consequently placed into the MSB scheme by default. Again these matters relate to characteristics of the schemes’ rules rather than things that are influenced by the structure or membership of the Trustees.

Possible future changes to the schemes’ rules

23. The DFRDB Authority notes that policy responsibility for the DFRB and DFRDB scheme rules resides with the Defence portfolio and that no changes to scheme rules affecting the superannuation entitlements of DFRB or DFRDB members are proposed in the Bills.
24. There is no existing requirement that the DFRDB Authority agree, or be consulted, regarding changes to the DFRB Act or DFRDB Act. On this basis the retention of a separate Board to administer military superannuation would not necessarily be more beneficial to members if significant rules changes were proposed in future.

Administration services provider

25. The DFRDB Authority notes that under the current legislative framework, DFRB/DFRDB members’ administration services are already provided by a single service provider. The DFRDB Authority also notes that on 26 November 2009, the Minister for Finance and Deregulation announced that the Australian Government will, from 1 July 2012, “*outsource the administration services of PSSap*”⁶.

⁶ Media Release 80/2009: The Minister for Finance and Deregulation

26. This means that the CSC will in due course need to engage and oversee a second administration service provider (in addition to ComSuper which will continue to administer the military and civilian defined benefits schemes) which has the potential to impact the resources available to oversee the DFRB and DFRDB schemes.
27. However, the DFRDB Authority accepts that this is a resourcing issue that the CSC will be required to manage in conjunction with the relevant policy Departments (the Department of Defence and the Department of Finance and Deregulation).
28. The DFRDB Authority notes that under the current arrangements its Chair is also the Commissioner for Superannuation, the CEO of ComSuper (the provider of administration services). The DFRDB Authority considers that the Commissioner discharges this dual responsibility without favour to the DFRDB Authority or detriment to any of the other civilian and military schemes administered by ComSuper.
29. On this basis the proposed establishment of ComSuper as a statutory agency, separate to the CSC, is considered unlikely to have a material impact on DFRB/DFRDB members and in fact would remove the need manage this potential conflict.
30. The DFRDB Authority also notes that the CSC may appoint its own staff to provide administrative and secretariat support. The DFRDB Authority currently relies on administrative support provided by the Commissioner for Superannuation and staff of ComSuper. In undertaking its functions in relation to the DFRB and DFRDB schemes in future, the CSC will not be reliant on such external support.

Administration service standards

31. The DFRDB Authority (represented by ComSuper), along with the MSB Board Executive Unit, is a party to regular negotiated agreements with the Department of Defence in relation to the funding made available to ComSuper to deliver administration services for the DFRB and DFRDB schemes. This agreement also specifies standards for such services.

32. ComSuper is required under these agreements to provide a higher standard of service to members of the military schemes (the standards for DFRB, DFRDB and MSB schemes being similar) in some areas than for the civilian schemes.
33. Examples of this are the maintenance of a separate call centre for military members and a requirement to answer calls in a faster time than the existing standard for the civilian call centre. Military member education seminars, and one-on-one education sessions, are also conducted in all States and Territories.
34. Future funding and service agreements with the Department of Defence will be negotiated by the CSC and ComSuper, which will also set service standards for the members of the civilian schemes. It is possible, and indeed likely, that there will be some harmonisation of service standards.
35. The DFRDB Authority also notes that it would be incumbent on the CSC to seek to negotiate acceptable standards of administration within the funding available and there is no suggestion that the standards currently applied to the civilian schemes are unacceptable.
36. On balance, the DFRDB Authority believes that DFRB/DFRDB members, former members and their associations are sufficiently informed and vocal that any diminution of service standards or lack of attention to issues will be brought to the attention of the Australian Government and CSC.

Conclusion

37. The DFRDB Authority notes assurances in the Explanatory Memorandum to the Governance of Australian Government Superannuation Schemes Bill 2010 that:

“ ... the single trustee has a responsibility to act in the best interests of all members. Accordingly, civilian and military interests are represented on its governing board. Importantly, consolidation will not affect members’ superannuation benefits in any way. Each scheme will retain its own legislative base and provisions.”

38. While there may be a perception that the transfer of Trusteeship of the DFRB/DFRDB to the CSC may erode consideration given to the unique nature of the military service, for the reasons given above the DFRDB Authority does not consider this to be a likely outcome.
39. In terms of practical changes, the proposed membership of the CSC includes two members (out of ten) nominated by the Chief of the Defence Force. The Explanatory Memorandum to the Governance of Australian Government Superannuation Scheme Bill 2010 also notes the intention that the Finance Minister would consult with Ministers in the Defence Portfolio in selecting the five “*employer directors*”⁷.
40. The changed arrangements also provide a discretionary power for the CSC to establish a DFCAC (with membership including three members nominated by the Chiefs of the three Services) to review decisions referred to it by the CSC.
41. While the internal operations of the CSC will be a matter for its consideration in due course, the DFRDB Authority notes that it is open to the CSC to appoint policy committees for each of the schemes if considered appropriate or necessary.
42. In the context of the above, the DFRDB Authority accepts the assurances of the Australian Government that the interests of DFRB and DFRDB members will be appropriately represented by the CSC. Therefore it is the view of the DFRDB Authority that it is not necessary to retain a separate board to administer the military superannuation schemes.

Do the military schemes differ markedly from other Commonwealth Government administered schemes?

43. The DFRDB Authority notes that there are substantial and well documented differences between the DFRB/DFRDB (and indeed the civilian defined benefits schemes) and the civilian accumulation scheme the Public Sector Superannuation Accumulation Plan (PSSap). Subsequent discussion is confined to a comparison of the DFRB/DFRDB schemes with the civilian defined benefits schemes only.

⁷ The remaining three directors being nominated by the Australian Council of Trade Unions.

44. As the DFRDB Authority does not administer the civilian defined benefits schemes, similarities and differences in schemes will be discussed only in broad terms. The Committee should take account of any corresponding submission by the Australian Reward Investment Alliance⁸.

Similarities to the civilian defined benefits schemes

45. The DFRB and DFRDB schemes are similar to the civilian defined benefits schemes in many respects. They are complex defined benefits schemes which are closed to new members. Members are required to make an employee contribution to the schemes and benefits are broadly based on remuneration on separation and years of service.
46. Administration of the DFRB and DFRDB is complex and costly but not markedly different in most respects to the civilian defined benefits schemes. Similar challenges exist in administering demographic shifts in membership. For example, maintaining a minimum level of expertise in the DFRB as membership is made up of pensioners (the majority of whom are surviving spouses) is equally a factor for the older civilian defined benefits schemes and is an emerging issue for the newer schemes.
47. Like the civilian defined benefits schemes, there is significant complexity in administering superannuation splitting of DFRB and DFRDB entitlements under Family Law arrangements.

Differences to the civilian defined benefits schemes

48. The DFRDB Authority considers that there are five significant differences between the DFRB/DFRDB and the civilian defined benefits schemes:
- a. Rate of Member contributions and absence of investment fund;
 - b. Ability to join another Commonwealth Government scheme in order to make ancillary contributions;
 - c. Re-entry to the ADF and the DFRDB;
 - d. Access to benefits after 20 years service; and
 - e. Relative complexity of invalidity retirement benefits.

⁸ The current Trustee for all of the Australian Government's civilian schemes.

49. As noted earlier, DFRDB members who are currently serving in the ADF must make an employee contribution. That contribution is standardised at 5.5% of the highest increment of the member's rank plus allowances. The contribution flexibility that exists in the civilian defined benefits schemes is absent because DFRDB member contributions are not invested for the member.
50. DFRB contributions are placed in the CRF and do not affect the final benefit received by the member i.e. unlike the civilian schemes, the DFRDB is a fully unfunded defined benefits scheme.
51. While the rate of contributions for DFRDB members are fixed, these members may make ancillary contributions⁹ to the MSB scheme in order for these additional contributions to be invested and managed (by the MSB Board).
52. In making these contributions, these DFRDB members become members of a second scheme for that limited purpose. The DFRDB Authority understands that civilian defined benefits scheme members do not have the option of making additional contributions to a second Australian Government defined benefit scheme while retaining full membership of the first.
53. The DFRDB provide for former ADF Members in receipt of a DFRDB Scheme benefit who, on re-entry to the ADF, chose to rejoin the DFRDB Scheme. While the DFRDB Authority understands that provision for re-entry exist in the civilian defined benefits schemes, this condition is more likely to be accessed by former ASDF personnel and is a significant source of complaints in its application.
54. In broad terms the rules are that DFRDB members who leave the ADF and receive a refund of their contributions must, when re-entering the ADF, join the MSB scheme. However, those members who are receiving a DFRDB pension who resume continuous full-time service of 12 months or more may elect to re-join the DFRDB scheme provided they make a signed election before the first day of that service. DFDB pensioners who resume on other than continuous full-time service for 12 months or more continue to receive their DFRDB pension and do not need to contribute to the scheme.

⁹ Government (Super) Co-contributions, Additional Personal Contributions, Salary Sacrifice Contributions, Spouse Contributions and Transfer Amounts.

55. There are issues of timing of members submitting elections and members resuming duty on several occasions with under different conditions (breaks in service or not). These issues are complex to administer and are the largest single source of complaints received by the DFRDB Authority.
56. Another difference is that unlike members of the civilian defined benefits schemes, DFRDB members are entitled to access benefits after 20 years service i.e. there is no compulsory preservation age. For this purpose “service” can also include can include non-ADF service.
57. As noted earlier, there are significant differences between the DFRDB scheme invalidity retirement rules and those of the civilian defined benefits schemes. The Australian Defence Force has the right to retire members on the grounds of invalidity if they do not meet strict medical standards - even though they may be capable of civilian employment of a similar nature. The DFRDB scheme rules provide for a scaled system of invalidity classification with correspondingly scaled benefits.
58. The DFRDB scheme rules take into account a member’s skills, qualifications and experience, and their retirement impairment in determining their incapacity for civil employment and establishing the appropriate invalidity classification. An A, B or C classification of invalidity is determined dependent upon the extent of the member’s loss of capacity to undertake appropriate civilian employment. Class A and Class B classifications denote, respectively, significant and moderate incapacity and attract different levels of pension. Class C classification reflects a comparatively small incapacity and a lump sum rather than a pension is payable to the member.
59. The determination of benefits payable to members who retire from the ADF as medically unfit for further service is a major component of the DFRDB scheme’s administration.
60. The DFRDB Authority understands that invalidity retirement requirements for the civilian defined benefits schemes are fundamentally different in that a civilian employee must be shown to be unable to be employed in a field which he/she would ordinarily be suitably skilled and trained to occupy (including at a lower level).

- 61. It is understood that the civilian defined benefits schemes also provide for partial invalidity arrangements i.e. where an employee receives a superannuation pension while remaining in the workforce at a lower rate of remuneration.

- 62. Aside from the significant case workload in administering these military invalidity provisions, there is also a need to undertake liaison with other agencies when benefits are affected by changes to rates of pensions (such as payments from the Department of veterans Affairs and Centrelink or tax issues affecting the ATO) and sensitively manage the impact of changes (such as reductions in benefits).

- 63. In cases of military invalidity benefits, it is also perhaps more likely that members may have conditions affecting the way in which such benefits issues must be communicated (e.g. Post Traumatic Stress Disorder).

Conclusion

- 64. There are significant differences between the DFRB/DFRDB Schemes. There is no doubt that these differences affect the manner in which administration the rules is carried out and in the cost of that administration. The DFRDB Authority considers there is also a need to provide some assurance to members that there is an oversight of decisions in applying these rules by a body that includes experience with ADF conditions and issues.

- 65. However, the DFRDB Authority considers that the membership arrangements for the new CSC, and those for the new DFCAC, adequately reflect the needs of military representation in these matters. In addition the Department of Defence will continue to be closely involved in setting administration service standards and ComSuper will continue to be the provider of those services (albeit with some changes to its agency status).

- 66. The DFRDB Authority considers that there are insufficient differences in scheme rules between the DFRB/DFRDB schemes and the civilian defined benefits schemes to warrant maintaining a separate military Board.

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