Chapter 2

Civilian Superannuation

Background

2.1 The Superannuation Legislation Amendment Bill 2007 (the bill) is designed to reduce some of the complexities surrounding public sector superannuation, and remove certain rigidities associated with the Commonwealth Superannuation Scheme (CSS) and Public Sector Superannuation Scheme (PSS). The bill is intended to provide members 'with the same flexibility and incentives to contribute to superannuation that are available to the broader community'[1] and thereby remove some disincentives associated with public sector employment.[2]

2.2 There are currently three major Commonwealth public sector superannuation funds:

- CSS;
- PSS; and
- Public Sector Superannuation accumulation plan (PSSAP).

2.3 The CSS is a hybrid scheme, the PSS is a defined benefits scheme, and the PSSAP is an accumulation fund. The Australian Reward Investment Alliance (ARIA) is the trustee that manages the schemes, while ComSuper is responsible for the day-to-day administration of the schemes.

Voluntary contributions

2.4 Schedule 1 of the bill removes, from 1 July 2008, the mandatory requirement for members of the CSS to pay five per cent of their post-tax salary as a basic contribution to the scheme. Instead, the bill proposes that member contributions be voluntary, permitting members to elect to pay zero per cent basic contributions. The Department of Finance and Administration (Finance) estimates that only a very small proportion of CSS members will take up this option.[3]

2.5 Similar changes are proposed to be made for the PSS. The PSS currently requires members to pay contributions of between 2 and 10 per cent. However, amendments to the *Superannuation Act 1990* (PSS Act) are not required as the

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1 The Hon. Gary Nairn MP, Special Minister of State, *House of Representatives Hansard*, 21 June 2007, p. 8.

2 Department of Finance and Administration, *Submission 6*, p. 3.

3 Ms Campbell, Deputy Secretary, Department of Finance and Administration, *Committee Hansard*, 5 July 2007, p. 21. Finance's estimate for the number of people in the CSS expected to reduce contributions is based on a zero per cent actuarial assessment.

changes to the PSS will be made by a PSS Amending Deed.[4] Finance estimates that approximately 10 per cent of PSS members will take up this option.[5]

2.6 A number of organisations expressed concern that some members may be disadvantaged by opting to make zero per cent contributions to their scheme. A member may choose to receive their benefit as an indexed pension, a lump sum, or a combination of both. The schemes have an accumulation component which is used to calculate a member's lump sum payment; this is based on the member's contributions plus earnings, less tax. In this context the Superannuated Commonwealth Officers' Association (SCOA) commented:

> Should the member opt to cease contributions to the CSS, the lump sum will continue to grow but the ultimate lump sum will be less.[6]

2.7 At the public hearing, SCOA cited an article by Mr Daryl Dixon, chairman of Dixon Advisory and Superannuation Services, which provides an example in real dollar figures of how a member could be disadvantaged by reducing their contributions to zero per cent:

> …he estimated the reduction in the pre-age 55 retirement pension of a person aged 45 at present—so with 10 years to run—who is earning currently $50,000 a year. The loss was estimated to be in the order of $800 for every year that no contribution was made to the CSS. So in 10 years you could accumulate—in reverse…an $8,000 reduction in your pension that you would otherwise have had at age 55. That is a very substantial drop in pension for quite a modest income earned of $50,000.[7]

2.8 Mr Dixon expanded on these concerns in his article:

> To the extent that CSS members reduce their contributions below the basic 5 per cent level in the future, they will be shooting themselves in the foot by reducing the potential value of a future preservation benefit from the fund.[8]

2.9 The committee notes a number of submissions recommended that members be adequately informed of the proposed changes to the PSS and CSS, and the impact that zero per cent contributions will have on their future benefits. This issue is discussed in chapter 4 under, 'Informing members of changes to superannuation'.

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4 Explanatory Memorandum, pp 2, 3 and 10. The PSS Amending Deed is a delegated legislative instrument made by the Minister for Finance and Administration which is subject to Parliamentary disallowance.

5 Ms Campbell, Deputy Secretary, Department of Finance and Administration, *Committee Hansard*, 5 July 2007, p. 21. Finance's estimate for the number of people in the PSS expected to reduce contributions is based on the number of members currently making the minimum contribution of 2 per cent.

6 Superannuated Commonwealth Officers' Association, *Submission 1*, p. 8.

7 Mr Hazell, Federal President, Superannuated Commonwealth Officers' Association, *Committee Hansard*, p. 2.

8 Mr Daryl Dixon, 'Now for the July 2008 super changes', *Canberra Times*, 3 July 2007, p. 33.

Choice of fund for PSS members

2.10 Currently, PSS members can only cease contributing to the scheme upon leaving employment or retirement. In addition, when former members return to the public sector they must also return to the scheme from which they left, regardless of the amount of time they have not been contributing to that scheme.[9]

2.11 Schedule 2 of the bill will allow, from 1 July 2008, for PSS members to cease membership of the scheme and choose to make contributions to another scheme while retaining a preserved benefit in the PSS. The bill also amends the *Superannuation Act 2005* (PSSAP Act) to allow eligible PSS members to elect to join the PSSAP. PSS members who choose to leave the scheme are not eligible to return to the PSS at a later date.[10]

2.12 Finance outlined in their submission that this entitlement was not made available to members of the CSS as they had been given the opportunity to leave the fund and transfer to the PSS in 1990 and 1996. Further, due to the differences between the defined benefit structure of the CSS and the PSS, a decision to re-invite members of the CSS into the 'choice of fund' environment would have significant budgetary impacts.[11]

2.13 To cease membership of the PSS and join another fund, a member must apply in writing to ARIA. Further, the member must be eligible to join the PSSAP, or have a chosen fund that is accepted by the employer, and be a member who is making contributions to the PSS (this excludes members with only a preserved benefit in the PSS).[12]

2.14 A member's eligibility to join another superannuation arrangement will be determined by the choice arrangements that their employer has in place. Where a PSS member elects for a 'choice of fund', they will usually become a PSSAP member in the first instance, with the ability to then cross over to another fund.[13]

Requirement to transfer to PSSAP

2.15 The committee asked Finance why members electing for 'choice of fund' were required to join the PSSAP before they were permitted to join another fund.

2.16 Finance told the committee that PSSAP is the default superannuation scheme for employees of the Australian Public Service. The requirement for members to join PSSAP in the first instance was the simplest way to place members in the 'choice of

9 Department of Finance and Administration, *Submission 6*, p. 5.

10 Department of Finance and Administration, *Submission 6*, p. 5.

11 Department of Finance and Administration, *Submission 6*, p. 6.

12 Explanatory Memorandum, p. 13.

13 Explanatory Memorandum, pp 2 and 13.

fund' environment from a statutory perspective. To enable 'choice of fund' directly from the PSS would require complex changes to the PSS Act, whereas PSSAP is already established within the 'choice of fund' framework. Once a member of PSSAP, an employee can opt to join another scheme.[14] In effect, PSSAP is being used as a gateway for members to enter the 'choice of fund' environment.

Disadvantages of leaving the PSS

2.17 SCOA noted in their submission that some members could be disadvantaged by leaving the PSS:

> Those who leave the PSS will lose the matching employer contribution as well as the Government co-contributions. This would need careful balancing against the payment of contributions at the marginal tax rate…Importantly many may not have the knowledge to recognise it.[15]

2.18 This option may not be advantageous to the majority of members, whereas some may find the new found flexibility suits their personal circumstances. For example, those who desire to take a higher level of investment risk may choose to move to an accumulation fund,[16] or those with a terminal illness may have little use for the pension provided by the PSS and prefer to move to a fund that will give a greater lump-sum payout.[17]

2.19 The committee notes the recommendations from a number of organisations to ensure members are fully informed about the proposed 'choice of fund' entitlement and the impact that leaving the PSS would have on their future benefits. This issue is further discussed in chapter 4 under 'Informing members of changes to superannuation'.

Pension restoration

2.20 Schedule 4 of the bill provides, from 1 January 2008, for the prospective restoration (upon successful application) of pensions for persons who have previously had their spouse pensions cancelled upon remarriage. This amendment only affects pensioners under the civilian scheme prior to 1976 which was then governed by the

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14 Department of Finance and Administration, *Submission 6*, pp 5–6; and Mr Sotiropoulos, Assistant Secretary, Department of Finance and Administration, *Committee Hansard,* 5 July 2007, p. 18.

15 Superannuated Commonwealth Officers' Association, *Submission 1,* p. 5.

16 Mr Leslie Nielson, 'Superannuation Legislation Amendment Bill 2007', *Bills Digest*, No. 2, 2007–08, 18 July 2007, p. 13.

17 Mr Hazell, Superannuated Commonwealth Officers' Association, *Committee Hansard*, 5 July 2007, pp 4–5.

Superannuation Act 1922 (1922 Act).[18] The 1922 Act predates the CSS and PSS, and therefore members of the PSS and CSS are not affected by these amendments.

2.21 Once satisfied that a person's application is valid, the Commissioner for Superannuation must grant full restoration of the pension at the same rate the person would now be receiving, had the pension never been cancelled. If an application is received on or after 1 January 2008, the pension will be reinstated from the date the application is received by the Commissioner. If an application is made before 1 January 2008, if granted, the pension is payable only from 1 January 2008 as specified in the bill.[19] The pension is restored on a prospective basis and therefore, pensioners are not reimbursed for the period of time pre-dating their application.

2.22 This amendment is likely to impact on a small number of pensioners that exist under a scheme that pre-dates the CSS and PSS. SCOA told the committee that there are in total approximately 8000 pensioners currently benefiting from the 1922 scheme, aged between 50 to over 100. Based on these figures, SCOA estimates there would be no more than a few thousand people eligible to apply for the restored pension in a similar age bracket.[20]

2.23 Finance informed the committee that they have no record of the number of pensioners eligible for the restored pension, nor records of contact details, and it is therefore difficult to estimate an overall number. However, Finance expects that there would only be a small number of eligible persons.[21]

2.24 A number of organisations highlighted the difficulties that having no contact details for the pensioners would pose in alerting eligible remarried pensioners to their restored entitlement. In addition, many of the pensioners would not have had contact with ComSuper for many years, and perhaps decades. SCOA, the Community and Public Sector Union (CPSU) and the Regular Defence Force Welfare Association (RDFWA) argued that extra measures be taken to alert these pensioners to their restored entitlement. This matter is further discussed in chapter 4 under, 'Informing members of changes to superannuation'.

2.25 In addition, SCOA recommends that due to the amount of time it would take to locate the beneficiaries of this provision, all successful applicants should be

18 It also applies to military pensioners under the *Defence Force Retirement Benefits Act 1948* and the *Defence Force Retirement and Death Benefits Act 1973* prior to the 1977, which is discussed in chapter 3.

19 Explanatory Memorandum, pp 2 and 19.

20 Mr Hazell, Federal President, Superannuated Commonwealth Officers' Association, *Committee Hansard*, 5 July 2007, pp 3 and 6.

21 Ms Campbell, Deputy Secretary, Department of Finance and Administration, *Committee Hansard*, 5 July 2007, p. 18.

reinstated their pension from 1 January 2008 regardless of when their application is lodged.[22] This matter is explored further in chapter 4 under, 'Restoration of pensions'.

Early release of benefits

2.26 From 1 January 2008, Schedule 3 of the bill will enable CSS members to obtain early release of their accumulated funds on 'severe financial hardship' and 'compassionate grounds' as defined under the *Superannuation Industry (Supervision) Regulations 1994* (SIS Regulations). Amendments to the PSS Act are not required as the changes to the PSS will be made by a PSS Amending Deed.

2.27 These amendments are required to bring CSS and PSS member entitlements into line with that of the broader community, as the early release provisions of the SIS Act and SIS Regulations do not operate automatically within the CSS and PSS. In order for the provisions to operate in a particular scheme, the early release provisions must be explicitly included in the rules of that scheme.[23]

2.28 The committee supports these amendments.

Amendments relating to the Government's *Better Super* reforms

2.29 Schedule 5 of the bill seeks to make consequential and technical amendments arising from the Government's *Better Super* reforms provided in the 2006–07 Budget and to provide consistency with the arrangements for the broader community. The main amendment will ensure the continued payment of employer productivity contributions for a member who cannot make member contributions because they have not provided their tax file number.[24]

2.30 The committee supports these amendments.

Other matters raised during the inquiry

2.31 A number of matters not directly related to the provisions of the bill were discussed by various organisations. These matters are briefly addressed below.

Interdependency

2.32 The CPSU argued that, unlike most private sector schemes, a partner in an interdependency (including same-sex) relationship is excluded from receiving a reversionary pension benefit on death of a CSS or PSS member, and that this should be rectified. The union argued that the amendments proposed by the bill do not adequately address the issue.

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22 Superannuated Commonwealth Officers' Association, *Submission 1*, p. 9. This matter is also raised by the Regular Defence Force Welfare Association and is further discussed in chapter 3.

23 Explanatory Memorandum, pp 2 and 15.

24 Explanatory Memorandum, p. 2.

2.33 The CPSU argued that whilst a reversionary pension benefit would become available to these members in the 'choice of fund' environment, those leaving the PSS would still be required to retain accumulated funds in the PSS. The union was concerned that certain benefits in the employee's new scheme would become progressively available only as funds accumulated. Further, the CPSU argued that funds retained in the PSS would still be unavailable to members in an interdependency relationship seeking a reversionary pension benefit.

2.34 The union endorsed the recommendations made by the Human Rights and Equal Opportunity Commission (HREOC) in its recently published report, *Same-Sex: Same Entitlements.*[25] The HREOC recommendations relating to superannuation stated:

> The inquiry's preferred approach for bringing equality to same-sex couples is to:
>
> - retain the current terminology used in federal legislation (for example retain the term 'spouse' in the Superannuation Act 1976)
> - redefine the terms in the legislation to include same-sex couples (for example redefine 'spouse' in the Superannuation Act 1976 to include a 'de facto partner')
> - insert new definitions of 'de factor relationship' and 'de facto partner' which include same-sex couples.[26]

2.35 The committee observes that providing a reversionary pension benefit to those in an interdependent relationship is not the explicit intention of the bill. However, the bill does alleviate the situation to some degree by allowing members of the PSS to accumulate future contributions in a fund that offers the reversionary pension benefit to employees in interdependent relationships.

Salary sacrifice

2.36 Both SCOA and the CPSU pursued their ongoing interest in allowing CSS and PSS members to salary sacrifice member contributions before tax (to align the CSS and PSS with the same tax concessions available to the general community). SCOA and the CPSU note in their submissions that rather than making this change, the Government has opted to give members the opportunity to leave the PSS entirely. The organisations do not believe this is a satisfactory solution.[27]

2.37 Finance responded to the issue:

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25 Community and Public Sector Union, *Submission 4*, p. 5.

26 Human Rights and Equal Opportunity Commission, *Same-Sex: Same Entitlements,* May 2007, p. 307.

27 Superannuated Commonwealth Officers' Association, *Submission 1*, p. 5; and Community and Public Sector Union, *Submission 4*, pp 4 and 6.

> The PSS and CSS come as a package deal. Members contribute post marginal tax salary. In the PSS they have a matching contribution provided by the government and the taxpayer and what are considered to be generous pension conversion factors and a reversionary pension. That comes as a package. Were the government to decide that those contributions were to be paid post the 15 per cent tax rate, that will come at an additional cost to the taxpayer.[28]

Other matters

2.38 Other matters addressed during the committee's inquiry include:

- Introduction of Transition to Retirement;[29]
- Changing CSS and PSS pension indexation from the Consumer Price Index to the Male Total Average Weekly Earnings;[30]
- Changing the taxation arrangements for employees in 'untaxed' superannuation schemes;[31] and
- Tax arrangements for military personnel following the *Better Super* reforms.[32]

2.39 The committee observes that the matters raised that were outside the scope of the bill may have fiscal implications. To avoid further delays in enacting the provisions of this bill, the committee does not believe it appropriate to address these issues in the bill.

28 Ms Campbell, Deputy Secretary, Department of Finance and Administration, *Committee Hansard*, 5 July 2007, p. 24.

29 Community and Public Sector Union, *Submission 4*, p. 4.

30 Community and Public Sector Union, *Submission 4*, p. 5.

31 Community and Public Sector Union, *Submission 4*, pp 5–6.

32 *Committee Hansard*, 5 July 2007, pp 25–26.