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The Honourable Dan Tehan MP
Minister for Veterans' Affairs
Minister for Defence Personnel
Minister Assisting the Prime Minister for the Centenary of ANZAC
Minister Assisting the Prime Minister for Cyber Security
Parliament House
CANBERRA ACT 2600

24 August 2017

Dear Minister,

I am writing in reply to your undated letter, emailed to me on 16 August 2017, which relates to my submission [The Gross Reduction of DFRDB Benefits](#), dated 16 February 2017.

The motivation for my reply is the very questionable content of your letter, in particular, the *parts* repeated below.

I note that you also wrote to the Prime Minister on 26 July 2017 regarding the same matter.

The Prime Minister would have received a copy of a letter in which I commented on Labor's position on DFRDB. As will be the case with this letter, it was circulated to every Senator and MP in whose State or Electorate DFRDB retirees reside.

Given the complexity of the concerns you and Mr Jim Hislop have raised, extensive research was required in order to provide you with an informed response.

I doubt that any extensive research was undertaken. Your response, has been 'cut and pasted' from the many similar responses, to DFRDB community concerns, which have been drafted by the Department of Defence. As has been the case in those previous responses, your response presents a *fait accompli*, that there will be no change made to the DFRDB arrangements, without addressing any of the evidence which disputes the validity of those arrangements. Your response then 'cherry picks' from the [Matthews Review](#) and the [Podger Review](#) and makes baseless comparisons with the DFRDB scheme in an attempt to justify that position.

That this response took 176 days (almost half a year) after Jim Hislop and I presented the submission in your Canberra offices, is a disgrace.

... the Defence Force Retirement and Death Benefits scheme was developed as a structure of elements. In assessing the overall benefit of the Scheme, it is not reasonable to consider individual elements of the Scheme as a change to one element changes the entire basis on which the Scheme was developed.

This has been a consistent statement in many of the responses to concerns raised by the DFRDB community. Yet, not one of those responses, including this one, has explained what the *entire*

basis on which the Scheme was developed constitutes and how a change to an individual element of the scheme would alter it.

The [Jess Report](#), which defined the DFRDB Scheme, contains nothing which suggests there is an inter-dependent relationship between the individual elements of the Scheme.

I can assure you that it is not the intention of the Government or administrators to deny recipients specific benefits that are provided for under the Defence Force Retirement and Death Benefits scheme legislation.

The failure to include a clause, in the Defence Force Retirement and Death Benefits Bill 1973, which restores retirement pay to full value after the life expectancy on which retirement pay reductions were based is reached, could have been an oversight. But on a balance of probabilities, it was intentional.

The exclusion, in the Defence Force Retirement and Death Benefits (Amendments) Bill 1977, of the part of the retirement pay entitlement which could have been commuted, from the indexation of benefits for; members who did not commute, spouses, dependent children and orphans, was deliberate.

[The Gross Reduction of DFRDB Benefits](#) contends that this was not necessarily the intention of the Parliaments of the day. Due the manner in which these Bills were hastened through Parliament, neither the Members of the House of Representatives nor the Senate had adequate time to properly scrutinize and consider these Bills.

At no point, before the closure of this scheme in 1991, were DFRDB members informed of the impact of these provisions and at no time since, has a valid rationale for their existence been put forward.

... the Government does not intend to make further improvements to the benefit structure of the Defence Force Retirement and Death Benefits scheme.

The DFRDB community is not seeking any further improvements to the benefit structure of the scheme. They are seeking a restoration of their benefits to the rightful level and the removal of the provisions which continue to reduce their benefits over time.

Indexation

There have been numerous reviews of indexation of all Commonwealth superannuation schemes, as well as specific reviews that have considered military superannuation schemes as a whole, over the past two decades.

In his review findings of the 2008 Review of Pension Indexation Arrangements in the Australian Government Civilian and Military Superannuation Schemes, Mr Trevor Matthews recommended there be no change to the indexation methodology for pensions paid from Commonwealth schemes. He concluded that the purpose of pension indexation for the Commonwealth schemes should be to continue to protect indexed scheme pensions from the effects of inflation and not to provide pensioners with a share of productivity benefits. The Government of the day accepted Mr Matthews' recommendations. His review findings remain relevant today.

It is not surprising that your response should focus on the widely discredited Matthews review. Of the many reviews of Commonwealth Superannuation scheme indexation, it was the **only one** which recommended that there should be no change to the indexation methodology.

Indexation is supposed to maintain the real value of benefits in line with community standards. But, as has often been the case, the Consumer Price Index (CPI) has been used by Governments to reduce benefits over time, because it is a well-known fact that the CPI fails to maintain pace with those community standards.

Recent evidence of this can be seen in Australian Government, [*Budget measures: budget paper no. 2: 2014–15*](#), 2014, page 203, which proposed to change indexation arrangements for the Age Pension, Veterans' Pensions, Carer Payment, Disability Support Pension and Parenting Payment, so that payment rates are only adjusted by movements in the CPI. A measure which was expected to *save* (for that read *reduce those benefits by*) \$449 million over five years.

[The Gross Reduction of DFRDB Benefits](#) demonstrates irrefutably that, after productivity gains have been removed, the indexed rates of benefits paid to members who retired before 1992 are substantially less than those paid to members who retired, or will retire, after 2015. Between 1991 and 2013, that difference was more than 25%.

Mr Matthews' review findings have *not* remained relevant.

The paper contends that the Abbott Government's change of the indexation method acknowledged that the use of the Consumer Price Index for adjusting Defence Force Retirement and Death Benefits was unfair. This is not the case.

To the contrary. That was precisely the case, as was clearly stated in *The Coalition's Policy for Fair Indexation of Military Superannuation*, dated July 2013, and why the Bill, which introduced the change in the Parliament, was named *The Defence Force Retirement and Death Benefits (Fair Indexation) Bill 2014*.

That Bill however, applied fair indexation only for beneficiaries aged 55 and over and did nothing to address the reduction of benefits suffered by those who were affected by *unfair* indexation for a period of 23 years up to 2014.

It is important to note that the Podger Review Team also concluded that the Defence Force Retirement and Death Benefits scheme is already a particularly generous scheme for those in receipt of pensions, that Consumer Price Index indexation does maintain purchasing power, and is generous when compared to most contemporary superannuation schemes that may only provide account-based pensions at the member's risk.

This perception of the generosity of the DFRDB scheme has long been cited as a major justification for not addressing the DFRDB community's concerns.

The Podger Review Team re-affirmed the view of the Cole Report and concluded that; while the DFRDB benefit after more than 30 years' service, at an age close to 55, provided a generous retirement income, a DFRDB pension for those who separated just after the 20 years qualifying period was never sufficient to provide an adequate level of retirement income to maintain the member's lifestyle, unless supplemented by post separation income and savings.

In its analysis of separation from the Defence Force versus years of qualifying service, the [Podger Review](#) shows that a vast majority of separations occurred after 20 to 22 years, indicating that this perceived generosity of the Scheme is not applicable to a large proportion of the DFRDB beneficiary population.

In its assessment of the DFRDB and MSBS schemes, the Podger Review Team determined that, while the MSBS scheme compares reasonably well with most overseas military schemes

and with other Australian schemes for ‘uniformed bodies’, it still fell well short of best practice contemporary superannuation.

The Podger Review Team rated the DFRDB scheme *well below* the MSBS scheme.

Although recommending improved indexation for older Defence Force Retirement and Death Benefits pensioners, the Review Team considered there is no case to increase the generosity of benefits payable to pensioners prior to age 55, given government policy on preservation arrangements.

The Podger Review Team determined that there was an in-principle case for changing the indexation arrangement for DFRDB benefits to an earnings basis, but recognised that the additional expense could not be absorbed within the envelope of the costs of current arrangements, which the Review Team had aimed to achieve. That is, the Review Team excluded DFRDB recipients under the age of 55 from fair indexation because it was constrained by its Term of Reference.

Commutation

With regard to the commutation provisions in the Defence Force Retirement and Death Benefits Act 1973, the understanding of how the provisions are to be applied is not correct. Whilst this may not be the outcome sought, evidenced by the undertaking of such extensive analysis as shown in the submission, however the choice to voluntarily commute results in a permanent reduction of the pension benefit. The Defence Force Retirement and Death Benefits lump sum payment is not a loan that is to be repaid, despite there being a misunderstanding by some that believe it to be a loan.

There is no misunderstanding. Whether the term used is; lump sum, loan, advance or pre-payment is both academic and irrelevant. [The Gross Reduction of DFRDB Benefits](#) demonstrates irrefutably, that members who elected to receive an advance lump sum payment have, in exchange, had imposed on them a disproportionately high reduction of their retirement pay.

The term *permanent* reduction does not appear in; the [Jess Report](#), the [DFRDB Act](#) or in any of the information pamphlets published by the DFRDB Authority before the closure of the scheme in 1991.

How were members supposed to know that, if they lived a normal life span, the outcome of their choice to voluntarily commute would be a permanent and therefore, disproportionately high reduction of their retirement pay?

Not only is this arrangement grossly unfair, the degree of disadvantage, which is determined by the date of death, relative to the date of reaching life expectancy, is not consistent across the 80% of members who commuted and have already survived or will survive beyond the life expectancy on which their retirement pay reduction was based.

Notional Rate of Retirement Pay

The paper suggests that the use of a notional rate of retirement pay should be removed from the legislation so that all of an un-commuted pension would be indexed. It should be remembered that automatic annual indexation was brought in around five years after the commencement of the Defence Force Retirement and Death Benefits scheme. In the five years prior to the introduction of automatic indexation, many retiring members commuted part of their pension to the maximum extent available to them. If indexation had been extended to the

non-commuted portion of a pension, it could be perceived that these members were detrimentally affected by the introduction of indexation as they did not have the benefit of considering the value that automatic indexation brought to the Defence Force Retirement and Death Benefits scheme. This also ensures that members who exercised the commutation option are neither advantaged nor disadvantaged relative to any other member of the scheme

This paragraph makes no sense at all. DFRDB benefits were increased by two one-time indexation adjustments during the **four** years prior to the introduction of automatic indexation. The only difference between the one-time and automatic indexation was the index used. Apart from the effects of the delay in implementing those one-time adjustments, no beneficiary of the scheme was either advantaged or disadvantaged relative to any other.

As already stated, the Defence Force Retirement and Death Benefits (Amendments) Bill 1977 excluded from indexation, the maximum part of the retirement pay entitlement which **could have been** commuted. The outcome was a **notional** (for that read **imaginary** or **fictitious**) rate of retirement pay which forms the basis for indexing the benefits for:

- Members who elected **not to commute**.
- Spouses and dependent children of deceased members, **for whom commutation is disregarded**.

[The Gross Reduction of DFRDB Benefits](#) demonstrates irrefutably, that the effect of this **notional** rate of retirement pay reduces considerably, the rates of these benefits over time.

The **notional** rate of retirement pay has no effect whatsoever, on the indexation of benefits for members who commuted to the fullest extent.

Re-entered Members

The claim that Defence Force Retirement and Death Benefits pension recipients who commute on discharge from the Australian Defence Force and who then re-enter for a further period of service are disadvantaged on subsequent discharge, is founded on the misunderstanding of the impact of commutation on the reduction in retirement pay.

Upon subsequent discharge from the Australian Defence Force, the initial commutation lump sum benefit is indexed to a 'future' value and then deducted from the re-calculated lump sum payable. This is to ensure that a re-entrant is not unduly advantaged or disadvantaged when compared with a member of the same rank who serves continuously.

Again, there is no misunderstanding of the impact of commutation on the reduction of retirement pay. The misunderstanding or otherwise, lies in the indexation of the lump sum benefit to a future value, taking no account of the impact on the reduction of retirement pay. The outcome of which, results in even greater disparity between the second commutation lump sum payment and subsequent permanent reduction in retirement pay.

Other Comments

The Defence Force Retirement and Death Benefits scheme was designed 45 years ago, prior to the introduction of some of the most significant superannuation changes in Australia. The unique nature of military service and therefore the special nature of the Scheme in meeting the requirements of the Australian Defence Force, places the Scheme outside mainstream superannuation considerations in the broader community.

The DFRDB scheme was designed 45 years ago to meet the requirements of the Australian Defence Force *then*. It was a *condition of service* for every serving member of the Defence Force who transferred from the DFRB scheme and every member who enlisted in the Defence Force from 1973 to 1991.

Recent actuarial advice has provided a comparison of the value of benefits available in the Defence Force Retirement and Death Benefits scheme compared to the benefits available under the new scheme, ADF Super. The comparison was based on the assumptions of a male Australian Defence Force member who joined at age 20, served 20 years and exited age 40 on a salary of \$80,000.

No doubt, this particular demographic was chosen to demonstrate just how comparatively generous the DFRDB scheme is at that point. However, this is not a valid comparison. The DFRDB scheme was closed to new members in 1991, therefore the latest year, in which a DFRDB member, who joined at age 20, served 20 years and exited age 40, was 2011, 5 years before the commencement of the ADF Super scheme.

Why is the DFRDB scheme not compared with the other closed and superseded Commonwealth superannuation schemes of that era? Such as; the Commonwealth Superannuation Scheme and the Parliamentary Contributory Superannuation Scheme? The reason is obvious. Those schemes are substantially more generous than the DFRDB scheme, hence, any comparisons with them have consistently been ignored.

Minister, it is unlikely that you have read my 106 page submission [The Gross Reduction of DFRDB Benefits](#) and judging from this response, which has been prepared for you by your Department, you cannot possibly have an understanding of the DFRDB community's concerns.

Jim Hislop and I are prepared to travel to Canberra again, in the hope that you will give us an opportunity to put those concerns to you in person. Alternatively, we invite you to visit Wodonga and participate in a Q&A session in our local RSL Sub-Branch, which counts among its members, many DFRDB retirees. I assume the Member for Indi, Ms Cathy McGowan AO MP, would be delighted to adjudicate.

Yours sincerely,



Herb Ellerbock