Excessively Harsh Treatment of the Superannuation Pension of retired Commonwealth Public Servants' Defined Benefit Schemes such as the Commonwealth Superannuation Scheme (CSS)

The Retirement incomes of pensioners to the defined benefit schemes such as the CSS are treated very harshly and I am requesting you to highlight these harsh treatments in your report with a view to having these pensions treated less harshly. I do not know the exact number of CSS and similar pensioners but I expect it is more than 250,000. And all of them are suffering from this harsh treatment of their retirement benefits, which were a condition of their employment. I have attached to this submission a copy of an explanation from the Superannuated Commonwealth Officers Association of the operation of the CSS and PSS schemes and relevant facts. You will note it confirms that employers were required to make employer contributions on behalf of members in their employ (contrary to assertions by others).

There are several issues which I am asking you to address:

<u>The Taxation Issue</u>

CSS and similar pensions are taxable, whereas pensions for age 60+ for ordinary Superannuation pensions are tax free and have been so since 2007. Taxation of CSS and similar pensions should have been made tax free at that time too. This omission and its impact is inequitable. My CSS pension is about $50,000 pa but I lose about $20,000 in tax. (and I could really use this $20,00 pa). If CSS pensions were untaxed as are normal superannuation pensions, I and the other CSS pensioners would be able to enjoy the full value of our pensions as do the pensioners of normal superannuation funds.

The CSS pension scheme was used during earlier years ie pre 1980 (when unemployment was around 2%) as an incentive to encourage people to join the public service instead of private enterprise. The "quid pro quo" was that Public sector salaries at that time were about 20% less than for the equivalent private sector jobs.

Departments and Statutory Authorities were required to contribute 20% of the salaries of CSS employees to the Treasury (see SCOA explanation in the attachment). The Commonwealth received this funding and chose to invest it providing Government services **without tracking the value of benefits provided by that investment.** **<u>So the CSS is not unfunded</u>**

I have made representations to the relevant Ministers but they hide behind the false assertion that no contributions were made and hence no tax was paid and therefore the pensioners should pay tax. My response is that I know that Departments were levied approximately 20% of the salary of relevant employees and that at the time of my service 1962 to 1992, no superannuation fund Commonwealth or private sector paid tax either on contributions or on earnings. In any case the Commonwealth paying tax to itself is an accounting nonsense. If the Commonwealth did not make contributions, as alleged by current Ministers, why is it that the penalty is paid by the employees, it should be the Commonwealth paying any penalty.

<u>That CSS and similar pensioners pay tax on their superannuation pensions, whilst other superannuation pensioners pay no tax on their pensions is inequitable. Please recommend that CSS and similar Pensions should be made either tax free (preferred) or as a fall back taxed at a maximum of 15%.</u>

<u>Transfer Balance Cap Problem</u>

In 2017 the Government introduced a "**Transfer Balance Cap"**, this limits the amount of funds that a person can hold in tax free pension account. Despite the fact that CSS and similar pensions are taxable, they are included in this transfer balance cap and the amount credited to the Transfer Balance Cap. This cap is the amount of CSS pension (before tax) multiplied by a factor of 16. This is an outrageously high factor, compounded by the fact I lose 37% (47% less 10% tax rebate) in tax means the effective valuation factor is

25.4. The Superannuation Industry Supervision Act shows the Pension Valuation Factor for pensioners (aged 65 years plus) for pensions indexed at less than 3% as 10. Similarly, the Department of Social Security shows a pension valuation factor of 10. https://guides.dss.gov.au/guide-social-security-law/4/9/5/50

This excessive Pension Valuation Factor crowds out any other superannuation the pensioner may have purchased with after tax savings forcing it into the accumulation phase where it is taxed at 15% and is unable to be rolled over to their spouse when they die.

I request you highlight this issue and recommend that CSS and similar pensions be no longer taxed and that the Pension Valuation Factor is reduced from 16 to 10

The Reversionary Issue

The CSS pension is reversionary, with the surviving spouse receiving 2/3rds of the deceased's pension. When a CSS pensioner dies, the spouse continues to receive 7 payments at the deceased pensioners full rate before payments fall to 2/3rds for the remainder of the survivor's life. Under present arrangements the pension is valued at the rate at the time of commencement, ie 16 times the full rate not 16 times the ultimate 2/3rds rate, consuming an unfair amount of the survivor's Transfer Balance Cap. **This is clearly inequitable.** The previous relevant Ministers have conceded that this is an unintended and inequitable outcome, but have not yet rectified it.

Please highlight this inequitable issue and require it to be rectified.

The Adequacy Issue

There is an old saying that 2 can live as cheap as one, the converse of this is that it costs almost as much for one to live as a couple.

Whilst a couple live together in retirement, they share the cost of one dwelling, one car and other similar expenses. They share joint income from their respective superannuation pensions each with a pension from $1.6 million transfer balance cap each and maybe some funds in the accumulation phase (remember that CSS pensioners with their Pension Valuation Factor of 16 this isn't a lot). Then one of them dies. What was in the deceased transfer balance cap can be rolled over to the survivor but what was in the deceased's accumulation account cannot. Suddenly you have an 80 year old widow having to deal with the amounts that cannot be rolled over and having to live on a seriously reduced income but still having very much the same expenses for house, rates water electricity etc.

Please recommend that for a couple, where one dies the contents of all of their superannuation can be rolled over into the superannuation accounts of the survivor without diminution.

The Indexation Issue

The CSS is indexed in line with the Consumer Price Index (CPI) (typically 2% pa). This gives the illusion that the CSS pension would retain purchasing power, but the CSS pension is taxed and as we have a progressive income tax system, the increased payments get taxed at a rate that increases faster and so the purchasing power of a CSS pension progressively declines. The Centrelink aged pension is indexed in line with Average Weekly Ordinary Times Earnings (AWOTE) (typically 4%), a much fairer arrangement.

It is inequitable that CSS pensioners, all of whom gave the Government sterling service, are sentenced to a retirement of declining purchasing power, whilst Centrelink pensioners many of whom have given limited or no service to the Government enjoy a retirement with maintained purchasing power

Please recommend that CSS and similar pensions be indexed at AWOTE instead of CPI, similar to Centrelink Aged Pension.

HOW the CSS and PSS work

By Anne Willenborg, Annette Barbetti and Trevor Nock

Extracted from SCOA SuperTime Newsletter May 2014 and reproduced with the kind permission of the publishers SCOA Federal Council

We are regularly contacted by members asking about the functions and features of the CSS and PSS schemes, in particular about the pension, the spouse pension, also known as the reversionary pension, and how the schemes are funded and why their pensions are taxed.

We thought it would be useful to give you a summary style account of the basic workings of the two schemes.

The following is not meant to be a legal document and not financial advice, because SCOA is not licensed to provide financial advice.

It is merely meant as a guide to the very basic functions of the CSS and PSS.

The Commonwealth Superannuation Scheme (CSS)

The Commonwealth Superannuation Scheme (CSS) was established under the Superannuation Act 1976 "to provide superannuation services and products to eligible employees of the Australian government and participating employers".

CSS pension - there are two types

The CSS is a so-called hybrid scheme, meaning it is a combination of two types of funds, a defined benefit fund and an accumulation fund. When you retire as a CSS member, you will of course receive your indexed defined benefit pension, but in addition, you can choose to receive a non-indexed pension or a lump sum payout of your contributions plus any earnings.

Indexed pension

In very simple terms, your defined benefit pension is calculated using a formula based on your final salary, your length of contribution and your age when you retire. Your defined benefit pension is paid out of the Consolidated Revenue Fund, into which your employer made contributions on your behalf while you were working in the public service.

Your pension is paid as long as you live and is indexed by the CPI. If you pre-decease your spouse/partner he/she, if eligible will receive 67% of your pension, also for life and also indexed by the CPI.

However, when you retire, you have the option to reduce your own pension to 93% of the full amount, which will give your surviving spouse a higher pension of 85% of your pension.

Your pension is taxed, albeit with a 10% offset for those aged 60 and over.

Non - indexed pension

Whilst your employer made contributions to the Consolidated Revenue Fund on your behalf, under the scheme rules you also had to make member contributions as well.

A small part of your employer's contributions, the so-called productivity component, together with your contributions, were paid to what is known as the Commonwealth Superannuation Corporation and invested on your behalf.

This part of your benefit can be taken as either a lump sum or additional, non indexed pension, the non-indexed pension is also worked out according to a formula and paid for life. Your surviving, eligible spouse/partner receives 67% (or 85% see above) of your pension.

Whether you choose the lump sum or the non-indexed pension, these are tax free for those aged 60 and over as they are funded by money that has already been taxed.

Why is your defined benefit pension taxed?

Many CSS members are not aware that contributions are made to the Consolidated Revenue Fund on their behalf during their employment in the public service.

The size of the contributions is determined by actuarial calculations based on the number of current pension receipts, their age and life expectancy and the size of their pension. Over the years, this has been between 22% to 26% of salary. The money currently being paid to the Consolidated Revenue Fund by employers on behalf of CSS contributing members is used to pay for those who have already retired.

The employer contributions made to the Consolidated Revenue Fund were not taxed. If these contributions had been paid to a taxed superannuation fund, they would have been taxed, and you would not have to pay tax on your pension once you reach age60.

SCOA does not believe that it is fair that CSS pensioners should pay tax on their pension just because their employer contributions, which were considered part of your 'package', were paid to Consolidated Revenue rather than a taxed superannuation fund.

SCOA has been lobbying for several years to have this gross disadvantage overturned, so far without any success. However, we will continue our campaign and believe that we are making some progress.

The Public Sector Superannuation Scheme (PSS)

If you thought the CSS was complicated, let's take a look at the PSS. It doesn't get any easier or simpler!

The Public Sector Superannuation Scheme (PSS) was established under the Superannuation Act 1990 "to provide superannuation services and products to eligible employees of the Australian government and participating employers".

So far, so good. It was established when the CSS was closed to new members, and in addition to being the compulsory superannuation fund for permanent government employees (this was in the days before "choice of fund"), as opposed to the CSS, the PSS also allowed employees on part time or short term contracts to join.

Your PSS pension

Your PSS pension generally consists of three components including contributions made by you and your employer to the Consolidated Revenue Fund as well as the employer financial component payable at the time you retire and claim your pension.

Depending on the circumstances, A PSS retirement benefit can be taken as a CPI indexed pension, or a lump sum amount, or a combination of both.

As a PSS member, you may make a contribution equivalent to a minimum 2% of your after tax income. You can contribute more if you wish (up to a maximum of 10%), which will increase your 'accrued benefit multiple', one of the figures used to calculate your pension.

Your "productivity component" is part of the fortnightly contributions made by your employer on your behalf.

The formula used to calculate your final benefit is based on your contribution rate, your average final salary (last three years) and length of membership, known collectively as your "accrued benefit multiple"

Finally, this is the most significance difference between the CSS and the PSS, there is your employer financed component. This is paid by your employer and determined when you leave the PSS and claim your benefit. Its value is the remaining balance after your member and productivity components (plus investment earnings, as applicable) are deducted from your total lump sum benefit. In other words, it is the amount of money required to pay for your defined benefit pension for the rest of your life.

What is the role of the Futures Fund?

The CSS was closed to new members in 1990; the PSS followed in suit in 2005. As a result, the number of *contributing members* is diminishing and therefore the funds being paid to the Consolidated Revenue Fund, as described above, are also diminishing.

The Future Fund was established in 2006 to make sure the government of the day was able to meet its "*unfunded liability*". This is the amount of funds required to pay for every PSS and CSS pension in the next forty years or so. Under the legislation, the funds in the Futures Fund cannot be accessed until either the year 2020 or until the Fund has accumulated at least $140 billion. As at 31 December 2013, the Future Fund had $96.56 billion in funds under management.

ComSuper

As we wrote in the February 2014 issue of SuperTime, ComSuper is the government agency which is responsible for the *administration* of the CSS and PSS schemes. If you have access to the Internet, ComSuper has a section on their website set aside for CSS and PSS pensioners called "pensioner services online".

Call ComSuper to get an access number which enables you to log on to your own pension account where you change your payment details; update your address, check your pension payment history and view and print your indexation advice letters and much more.

If you would rather speak to someone about some aspects of your pension, you can call ComSuper on 1300 001 777.

Source: *css.gov.au; pss.gov.au; comsuper.gov.au*