

Chapter 1: Introduction

- 1.1 This report has been prepared by the Australian Government Actuary, Mr Peter Martin, FIAA, and members of his office at the request of the Department of Defence. It sets out estimates of the long term superannuation costs of the Military Superannuation and Benefits Scheme (MSBS) and the Defence Force Retirement and Death Benefits Scheme (DFRDB) that will be charged to the Consolidated Revenue Fund (CRF). The estimates are based on scheme data supplied by ComSuper (the schemes' administrator) as at 30 June 2008.
- 1.2 Estimates of the long term costs of military superannuation have been provided by the Australian Government Actuary in a series of reports since the commencement of the DFRDB on 1 October 1972. The most recent estimate of the long term costs of the DFRDB and MSBS was carried out using data as at 30 June 2005 and was presented in my report dated June 2006.
- 1.3 This report has been completed in accordance with the principles recommended in the separate actuarial paper 'The Financing and Costing of Government Superannuation Schemes'. That paper provides a full explanation of the methods used and the reasons for their adoption.
- 1.4 Three measures of long term costs are provided:
 - Notional employer contribution rate

This is the employer contribution rate that would be required to fund the defined benefits accruing over the next three years, on the basis that superannuation benefits are accrued uniformly over the period until a member exits from the scheme or reaches his or her maximum benefit limit, whichever occurs first. It represents the employment cost that arises from the superannuation schemes, and has been expressed as a percentage of the defined benefit superannuation salaries.
 - Projection of actual employer costs

This is a projection of the actual cash outlays payable annually by the Commonwealth in respect of superannuation benefits for ADF personnel. The cost, which is explained in paragraph 2.14, has been projected over the next 44 years and expressed as a percentage of gross domestic product.

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- Net present value of unfunded liabilities

This indicates the total level of the accrued Commonwealth liability for superannuation benefits in respect of service up to 30 June 2008 less the value of assets held by the schemes.

- 1.5 The purpose of the triennial reviews is to assess the financial position of the schemes over the long term. Estimates of the net present value of the unfunded liabilities have also been produced on an annual basis for inclusion in the Department of Defence Financial Statements. These annual estimates are calculated in accordance with Australian Accounting Standard AASB 119 and are not directly comparable to the estimates provided here.

ADF operational environment

- 1.6 The recent high operational tempo of the ADF has resulted in changes which affect superannuation costs. Most notably, it is likely to have led to the significant increase in the number of invalidity exits from the MSBS. Allowing for this effect in the valuation assumptions has increased the on-going costs for contributory members of the MSBS by the order of 10 per cent. There has also been an increase in the number of ADF personnel which results in a higher total salary base for superannuation purposes and hence higher dollar costs.
- 1.7 Remuneration reform has led to higher than expected increases in pay rates for ADF personnel and a number of retention pay initiatives have been introduced. Increases in pay rates translate into higher dollar superannuation costs. Retention pay initiatives are not included in the defined benefit superannuation salary, but do affect resignation rates, at least in the short term. They also affect the additional contributions required under the approach adopted to ensure compliance with the Superannuation Guarantee arrangements. These arrangements are discussed further in Chapter 2.

Same sex partners

- 1.8 The Government announced its intention to provide reversionary pensions, following the death of same sex partners, in Commonwealth superannuation schemes including the military schemes. Changes to the schemes had not been made as at 30 June 2008. The cost of this change is minor in the overall context of the schemes with an estimated increase in the unfunded liability of around \$30 million. In these circumstances, no explicit allowance has been made for this change in the estimates in this report.

Reviews of military superannuation arrangements

- 1.9 A review of military superannuation headed by Mr Andrew Podger was announced in February 2007. In its final report, the Review Team recommended the closure of the MSBS to new members and the establishment of a new accumulation scheme. The Review Team also recommended serving ADF personnel in the DFRDB and the MSBS and preserved members in the MSBS be offered the opportunity to transfer to the new accumulation arrangement and receive a transfer value in respect of their accrued benefits. A lower priority recommendation was to index DFRDB (including DFRB) pensions in a similar manner to age pensions.
- 1.10 Separately from the Review of Military Superannuation, a review of the pension indexation arrangements for Australian Government superannuation schemes, which include the military superannuation schemes, was carried out by Mr Trevor Matthews in the second half of 2008.
- 1.11 At the time of preparing this report, no decisions had been made on any possible changes to military superannuation arrangements. We have therefore prepared this report on the basis that there are no changes to military superannuation arrangements and the MSBS continues to be open to new members.

Future Fund

- 1.12 In 2006, the Government established a Future Fund to meet unfunded superannuation liabilities, contribute to national savings and increase net worth. It is intended that the unfunded liabilities of all Commonwealth superannuation schemes, including the military superannuation schemes, would eventually be covered by the assets of the Future Fund. However, since the assets of the Future Fund are not held by the schemes, the unfunded liabilities projected in this report have not been reduced to take account of the assets which may be held by the Future Fund. Similarly, the projected outlays have not been reduced to take account of any drawdowns from the Future Fund.

Compliance with professional standards

1.13 The report has had regard to the Institute of Actuaries of Australia Professional Standard 400 (Investigations of Defined Benefit Superannuation Funds) and complies with the Standard insofar as it deals with unfunded superannuation schemes. Professional Standard 400 is designed to primarily apply in the context of funded private sector defined benefit superannuation funds. The schemes under review in this report operate on an unfunded or substantially unfunded basis with an implicit Government guarantee. Given the different context, there are substantial sections of Professional Standard 400 that are not relevant to this report.