



ACPSRO

**Australian Council of Public Sector
Retiree Organisations**

Better targeting superannuation concessions

Submission from the
Australian Council of Public Sector Retiree Organisations

April 2023

Background

The Commonwealth Government has requested comment from interested stakeholders on the issues raised in its discussion paper on Better targeting of superannuation concessions which was released on 31 March 2023.

The Australian Council of Public Sector Retiree Organisations (ACPSRO) has a strong interest in this topic and provides the following submission in relation to the commentary provided in the discussion paper relating to Defined Benefit (DB) superannuation pensions.

About ACPSRO

ACPSRO, formed in 1997, provides a united voice on retirement issues relevant to Commonwealth, State and Territory public servants and Defence retirees who receive Defined Benefit Superannuation Pensions to which they had to compulsorily contribute from their after tax income. These issues impact upon the well-being of more than one million Australian households. The majority of these retirees provided front line services to the community including teaching, nursing, emergency services, transport services, energy, the provision of infrastructure, the needed administrative services to support these essential functions and the defence and security of our country.

ACPSRO seeks to ensure that any changes proposed to how DB pensions are taxed do not have any unintended consequences for members of these schemes. In this regard we have restricted our comments to the section of the consultation paper relating to Defined Benefit superannuation schemes on pages 14 and 15 of the Consultation paper.

Response to Consultation Paper

Before commenting on the specific questions raised in the consultation paper, ACPSRO would like to make the following observations in relation to those who are members of Defined Benefit schemes, particularly those who are members of unfunded schemes.

1. During the accumulation phase there is no fund from which to draw tax, nor is there any clear way to determine the value of a person's interest in such a scheme, beyond the after tax payments which may have been required as a member of the scheme and any contributions which may have been made on a concessional basis by the employer. As there is no fund any determination of the value held will be largely artificial and seeking to arrive at a return, which may then be subject to tax, for such an artificial value will add further complications.
2. Given that part of any accumulations held by a member of a Defined Benefit scheme may include after tax contributions it is considered critical that any calculations made specifically exclude the value of such contributions as there has been no concessional tax arrangements associated with that portion of a member's fund balance, however that balance may be determined.
3. Apart from the Future Fund, there are few other accumulations held by governments in relation to their Defined Benefit schemes. As such, is it the intention of these proposed tax changes to tax some proportion of the returns from that fund as they may relate to amounts held within the Future Fund to meet future Defined Benefit pension payments to a selected group of high income public servants?
4. Once a member of a Defined Benefit scheme enters the pension phase of that scheme it is highly likely that any high income recipient will already be paying a marginal rate of income tax which exceeds the proposed 30 cents in the dollar marginal rate for the

earnings of funds with in excess of \$3 million. The fact that marginal rates of tax, which are already higher than the proposed 30% tax rate, are already being applied to these members of a Defined Benefit scheme must be recognised in any determination of the tax liability under the proposed changes. To further tax incomes by the proposed 30 per cent tax rate would be imposing double taxation upon these Defined Benefit pension recipients.

5. High income Defined Benefit recipients do not receive the benefit of \$1.7 million of their determined fund balance being tax exempt. The tax is paid on this proportion of their determined fund balance must also be considered when assessing any tax liability under the proposed changes.
6. ACPSRO has previously raised problems with the issue of a fixed multiplier being applied to all fund members which takes no account of the actuarial reality for those fund members. In this regard we have included a copy of our previous submission on this concern which leads to an incorrect determination of the value of a Defined Benefit pension, particularly as a member ages. Again this aspect of existing arrangements needs to be fixed before being used within the process of determining a person's TSB under the proposed changes.
7. There is also the issue of the effective death taxes applying to Defined Benefit pensions. As a minimum there is a 33% reduction of the "capital" within a member's fund on death of the member, and then there is a 100% reduction in the remaining "capital" upon the spouse's death. Defined Benefit schemes therefore provide no residual bequest for future generations. These effective death taxes must also be considered when determining the TSB applying to a member of a Defined Benefit scheme and the tax liability which may be applied. This issue is particularly pertinent to the proposals presented in the Consultation paper if it is concluded by the Government to maintain a fixed multiplier when determining the value of a fund, as opposed to a multiplier that reflects the actuarial reality for a fund member.
8. Finally, members in receipt of a Defined Benefit pension are unable to change their situation when changes, such as those being proposed, are introduced which impact on their pensions. As such ACPSRO considers that existing Defined Benefit pensioners be grand fathered as part of any changes.

ACPSRO considers the above points are critical when assessing how the proposed changes are applied to the members of Defined Benefit schemes. They introduce significant complications into the operation of the proposals, and our experience has been that such complexity leads to significant unintended consequences.

Consultation questions

10. Do the existing valuation methods for defined benefit interests in the pre-pension phase (under the existing TSB definition) work appropriately for the purpose of calculating superannuation balances over \$3 million?

As identified above, the existing valuation methods are not appropriate for determining the TSB. These valuation methods take no account of the actuarial reality of a Defined Benefit pension, nor do those valuation methods reflect the existing tax arrangements applying to Defined Benefit pensions.

11. Do the existing valuation methods for defined benefit interests in the pension phase provide the appropriate value for calculating earnings under the proposed reforms?

As stated above the current valuation methods will not deliver fair and equitable outcomes for recipients of Defined Benefit pension under the proposed changes. While the consultation paper discusses the means of valuing the TSB of a DB pension, it makes no comment on how earnings from the scheme may be determined. Is it proposed to add an additional tax to the already inadequate CPI indexation which is applied to these pensions as this is the only measure of “earnings” which could be determined?

This issue is of particular relevance when comparing the position of a retiree receiving a DB pension which is already subject to income tax as compared to a retiree who has converted up to \$1.7 million into a tax exempt lifetime income stream which has been actuarial determined.

12. Are there any alternative valuation methods that should be considered for either pre-pension or pension phase defined benefit interests?

As indicated in our previous submission on determining the transfer balance cap for a Defined Benefit pension, the current valuation methods should reflect actuarial realities and also the existing taxation arrangements applying to such pensions. This is particularly relevant where some kind of assessment is made of the “earnings” related to a DB pension.

13. Are there any preferred options in providing commensurate treatment for defined benefit interests?

Given the complexities of determining the actuarial value of a fund and then the proposed earnings from that fund, and the current taxation arrangements applying to Defined Benefit pensions, we consider that the approach proposed in the Consultation paper are totally inappropriate and need to be deleted from the proposed changes.

14. What are the benefits and disadvantages to any alternatives?

We have no comment on this question, other than to say there is considerable risk of perverse outcomes from the proposals as they apply to those who are members of Defined Benefit schemes during both the accumulation and pension phase.