

Submission to:

VICTORIAN INDEPENDENT REMUNERATION TRIBUNAL (VIRT)

Review of Superannuation Arrangements for Victorian Members of Parliament

Preface

The Victorian Independent Remuneration Tribunal (VIRT) website notes that the Tribunal is responsible for setting remuneration for Members of Parliament (MPs), local councillors and executives in the Victorian public sector. To that end the Tribunal has, in recent years conducted reviews and made determinations in relation to salaries and allowances.

The Tribunal is now conducting a review and report on the superannuation arrangements for Victorian Members of Parliament under Parts 3 and 4 of the Parliamentary Salaries, Allowances and Superannuation Act 1969 (Vic) (PSAS Act).

The Tribunal's issues paper published 20 May 2020 in particular highlights that the report is to address potential inequalities and irregularities between the New Benefits scheme that covers existing and former MPs elected between 2 July 1996 and 9 November 2004 and the Accumulation Scheme that covers existing and former MPs first elected from 10 November 2004.

The issues paper also records that under section 39 (2) of the Improving Parliamentary Standards Act 2019 (Vic) (VIRTIPS Act), the tribunal is not to consider any option that would result in an existing MP or former MP being in an overall position that is less favorable than before the making of the report.

The opportunity to make a submission to assist in raising issues relevant to this review is welcomed.

The importance of independent decisions

The VIRT is to be commended for taking an analytical approach to demonstrating the varying retirement outcomes that may occur for Members of Parliament depending on when a Victorian MP joined the Parliament and which scheme they were eligible for.

As noted in the VIRT's 2019 Determinations, there is no obvious comparable role to that of an MP that would allow a judgement to be made on the superannuation scheme to apply to MP's. Therefore, detailed actuarial modelling that identifies any irregularities and or inequities that exist between the two available schemes based on when the MP was elected is appropriate.

The review may also serve as an opportunity to consider the transfer of responsibility for determining superannuation arrangements to the VIRT as it has already done for all other remuneration arrangements.

Shifting the review and determination of these important arrangements to be independent of the Government of the day may also help protect the process from inappropriate internal or external influence, bias and political positioning. As the next section of this submission demonstrates, such issues can become even more prominent in the lead up to an election.

The ongoing influence of the Federal Government

History suggests that in matters relating to public service remuneration and superannuation, most state and territory governments follow the lead of the Federal Government.

In a superannuation context, this can be seen during the 1990s when Federal, State and Territory governments undertook reviews of their public service superannuation arrangements primarily to address the increasing rate and amount of unfunded liabilities.

The Federal Government acted in 1990 closing the Commonwealth Superannuation Scheme (CSS) defined benefit and replacing it with a more modern defined benefit, the Public Service Superannuation Scheme (PSS). In 1996, the Victorian Government took similar action closing its Existing Benefits Scheme and replacing it with the New Benefits Scheme.

Searching online, you can still find some significant research and analysis performed by government departments and parliamentary committees when these changes were being contemplated.

By contrast, there is very little research to find regarding the changes that were made in 2004 to MPs superannuation arrangements, certainly not any analysis of how those changes would impact the superannuation benefits of future Members of Parliament compared to those that came before them. And the reasons for that can likely be found in what was occurring at the time at Federal level.

2004 was a Federal election year and with the election scheduled for October, then Labor Opposition Leader Mark Latham announced in February 2004 that if elected he would close the Commonwealth MP superannuation scheme to new MPs.

To avoid the issue becoming a significant election campaign difference, then Prime Minister John Howard reacted almost immediately along similar lines. By June 2004 legislation closing the Commonwealth MP Scheme to new MPs and instead directing them to an Accumulation Scheme with a 9% superannuation contribution had been passed. Again, it is important to note that this was done without any analysis on the impacts or differences in retirement outcomes for new MPs.

The consequences to the mostly labor held state parliaments of not following suit would likely have drawn heightened media attention and scrutiny, particularly given the weight of the Prime Minister's comments at the time:

*"I mean I would hope that after this announcement this afternoon that all of your cohorts in state capitals will be on the trail of every State Labor Premier to make sure they do exactly the same thing and that you will give them no peace until they do."*¹

In Victoria, the decision was made to close the New Benefits scheme to new Victorian MPs on and from 10 November 2004. In the Victorian Government Legislative Council Hansard from 3 November 2004, the Hon. W. R. Baxter is recorded as saying:

"We have this bill today because a populist opposition leader thought he would take a cheap shot and criticise the superannuation scheme. This is the result... We right here and now will not pay, but our successors are going to pay very dearly indeed for Mr Latham's cheap shot. It will denigrate the Parliament because it will further narrow the representation from a wide range of people in our community who feel they can offer themselves as candidates for election."

¹ The Hon John Howard MP, Prime Minister, Press Conference Transcript, Parliament House, Canberra, 12 February 2004

Possible options to consider

Without wanting to pre-empt the results of the VIRT's modelling of retirement outcomes between the New Benefits Scheme and the Accumulation Scheme, it is expected that the defined benefit would produce a superior outcome in almost all cases and particularly as the period of tenure used in the modelling increases.

It remains to be seen to what extent the VIRT make any recommendations to address the inequities that are demonstrated in the analysis, but one or a combination of the following may be appropriate to consider:

1. One workplace one scheme

The most immediate and definite approach to dealing with any inequities that may be identified by the PWC actuarial modelling between the New Benefits Scheme and the Accumulation Scheme would be to close the lesser of the two schemes and place all MPs on the same base entitlements.

Such an approach would satisfy the Act's requirement that this Review not result in a less favorable overall position for an existing or former MP. Additionally, it would address the anticipated superannuation inequity that MPs serving in the parliament today and elected/appointed, are performing the same role as their counterparts elected/appointed pre 2004 and therefore, their base remuneration and entitlements ought to reflect that, excluding of course any additional office an MP may hold.

This was last considered by the Hazell Review in 2012. At the time it concluded that while there was a need to bridge the gap between the different superannuation arrangements of current MPs, it would be unjustifiable to return all MPs to the previous scheme given prevailing community values and expectations.

Some 8 years later, the VIRT's actuarial modelling would appear to provide a sound platform from which to review the likely outcomes for members of each scheme. These calculations will invariably take into account the effect of the changes that have been made in the years since the Hazell review recommendations and may be able to comment on the impact those changes have had.

Reopening the New Benefits Scheme and allowing current MPs who missed the opportunity to join to buy-back in would certainly remove a remuneration package difference that has effectively created two classes of current MP. Arguably this is the only way to ensure a level playing field between all current MPs as compared to each other as generally speaking there are practical difficulties comparing to other jobs in the community given the uniqueness of the role an MP as outlined later in this submission.

2. Enhance the separation payment

Initially introduced in 2013 as a resettlement allowance and subsequently replaced by the separation payment in 2019, it is paid when MPs who meet the eligibility criteria leave parliament and are not members of the pre-2004 defined benefit schemes.

The VIRT has specifically sought to include this payment in their review because it was introduced to address a discrepancy between how the superannuation schemes operate and to facilitate

completion of an MP's parliamentary business and support them as they transition from working as an MP.

In its current form, the separation payment provides for a payment of:

- three months basic salary, if an MP serves one term or less; and
- a pro-rata sum between three and six months basic salary, if an MP served between one and two terms; and
- a maximum of six months basic salary, if an MP served two or more terms.

The VIRT's actuarial modelling should look to identify the extent to which this payment has been effective in addressing the inequity between the outcomes of the New Benefits Scheme as compared to the Accumulation Scheme.

It may be appropriate for the VIRT to consider making an alternative recommendation to the reintroduction of a single defined benefit scheme when the actuarial modelling is completed, to enhance the separation payment formula and maximum amount to:

- bridge/remove the gap between the two schemes; and
- continue to address the fact that MPs do not accrue any long service leave or annual leave over the course of their tenure that can be paid as a lump sum at the end of their employment. Where access to a superannuation benefit may be restricted, such as in the case of MPs attached to the Accumulation Scheme, the importance of the separation payment being set at an appropriate level to achieve its stated objectives cannot be understated.

3. Maximising contributions to and/or benefits from the Accumulation Scheme

The VIRT's issues paper notes that the compulsory employer contributions to the Accumulation Scheme is currently 15.5%. It also notes that with the changes to MPs base salary effective from September 2019 that the compulsory contributions will ordinarily exceed the concessional contributions cap.

Practically, the base salary and contribution rate limits the amount of additional employer contributions that could be made to the Accumulation Scheme in an effort to bridge the gap between the two schemes. However, if other submissions address additional contribution options they could be considered further.

If the Accumulation Scheme is to continue to apply, consideration could be given to undertaking a comparative calculation, for example at the end of employment by an MP attached to the Accumulation Scheme. The calculation could be performed by an actuary having regard to their contribution and benefit particulars to determine the comparable benefit they would have received as a member of the New Benefits Scheme. A formula basis could exist through which all or a portion of the difference is remunerated in an appropriate form, perhaps as an additional amount in the separation payment if it is practically difficult to make additional contributions to super.

MPs have a unique role

In a 2004 report, the Australian Senate's Finance and Public Administration Legislation Committee² noted that the rationale stated by the Commonwealth Department of Finance for the introduction of a defined benefit parliamentary Contributory Superannuation Scheme in 1948 were:

- entering Parliament often meant foregoing potential superannuation payouts from previous employers due to leaving that employer prior to retirement age;
- electoral and parliamentary demands reduced members' chances to re-establish careers when their parliamentary term was over; and
- the need to entice people to enter Parliament who would not otherwise come.

While the first issue has largely disappeared with superannuation now a basic benefit of employment in Australia, the latter issues remain and have arguably become more compelling than they were 70 years ago.

In its submission to the VIRT's Determination of Setting the Value of the 'Basic Salary' and 'Additional Salaries' For Members of the Victorian Parliament review in 2019, the Victorian Parliamentary Former Members Association (VPFMA) stated:

- Performance and competence do not protect a Parliamentarian from arbitrary dismissal. The Member of Parliament is subject to the will of the electorate and their individual performance as a Member carries lesser weight than the electorate's view of the performance of the Government or political party of which they may be a member.
- MPs have no "unfair dismissal" provisions to fall back on, and while in recent years, there has been the introduction of a form of retrenchment pay they remain subject to an arbitrary dismissal that applies in no other employment.
- Former MPs often have considerable difficulty finding work after leaving Parliament and their political career can be a factor against them.
- There is no defined career structure through which to advance. While there are prescribed higher offices, which do attract greater responsibility and higher remuneration, these cannot be accessed in a similar way to those in other professions. Performance and additional qualifications do not necessarily improve the opportunity to access these positions as they are essentially the gift of the political party which might consider other factors such as regional representation, factional balance, or the House of Parliament in which the Member sits in allocating the post.
- The balance between risk and reward... being a Member of Parliament can be a perilous career choice subject to sudden, arbitrary dismissal. This is a factor in deterring many potentially good candidates from seeking election to Parliament. It is true that there are Members who could earn significantly higher remuneration outside of Parliament, but it is equally true that there is a strong disincentive for others to take the risk of disrupting their current career for the prospect of a much less secure position and lower salary in the Parliament.

² Australian Senate Finance and Public Administration Legislation Committee report on the Provisions of the Parliamentary Superannuation Bill 2004 and the Parliamentary Superannuation and Other Entitlements Legislation Amendment Bill 2004

https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Finance_and_Public_Administration/Completed%20inquiries/2002-04/super_bills/index

The VPFMA provided case study examples demonstrating where hard working, dedicated Members lost their seats due primarily to the unpopularity of the political party they represented.

Members of Parliament may have a shorter and more uncertain working life than other public servants or employees in the private sector. Their salary packages are unlikely to include other benefits that many other employees may receive, such as annual leave, long service leave, sick leave and unfair dismissal protections as noted above.

Importantly, their work performance and the relevance of their personal life to their work is subject to far greater scrutiny than the average working Australian. It is of interest and analysis to a far broader group who can adversely influence an MP's ongoing employment such as their political party, the media, lobby groups, their constituency and community expectations at large.

These are important considerations relevant to the holistic nature of MPs remuneration entitlements and should be considered equally relevant to this superannuation review as they were to the recent VIRT salary and allowances review.

Unfortunately, there appears to be very little research available about the difficulties or otherwise that former MPs encounter when transitioning away from their political careers. Of course, some are entering retirement but for those who are not, there is a lack of information about how difficult it may be to resume employment, how long that takes and the roles they accept relative to their skills and experience.

Anecdotally, there are suggestions that the higher an MP has been able to rise through the ranks to senior positions such as say a ministerial role, the more likely opportunities in the private or even public sector may avail themselves. But as the tribunal would know, such positions are the few rather than the many and so for other MPs who have served their constituency, the road back to a normal life may be more challenging, potentially through no fault of their own.

While those attached to the New Benefits Scheme may be more comfortable to navigate this period given their superannuation entitlements, it is important for the VIRT to consider these issues and ensure that equally, MPs in the Accumulation Scheme have sufficient superannuation or departure benefits to not add unnecessarily to the financial, health, mental and other challenges that may be encountered during that transition.

To further illustrate the difficulties encountered by MP's when transitioning from parliamentary careers, it is intended to provide some further case studies to assist the VIRT in its considerations. These will be included in any subsequent written submissions provided after the PWC actuarial modelling is available.

Superannuation disadvantage suffered by women

It is widely accepted that retirement income outcomes for women in Australia are significantly and systemically less than those for men. Data from the Australian Bureau of Statistics confirm this and demonstrates that the gap increases throughout their working lives and that women in Australia retire on average with 53% less superannuation than men.

Illustrative of this point is the 2017 report commissioned by the Australian Services Union and the think tank Per Capita titled *Not So Super, For Women: Superannuation and Women's Retirement Outcomes*. It found that over 70% of women have estimated balances under \$150,000 while less than 38% of men do. Further, 23% of men have balances over \$500,000 while less than four percent

of women hold such balances. Conversely almost a quarter of all women have balances less than \$50,000.

The report went on to say that the structure of superannuation is an important underlying cause of this problem. Because superannuation contributions are a direct function of pay, the gender pay gap ensures that women's balances will be systematically lower. The most recent data from the Australian Bureau of Statistics (ABS) indicates that women's pay rates for equivalent work are 10% lower than men's, and women's total pay across the workforce (adjusted for fewer hours worked) is 31% lower.

Whilst this may not be the case in relation to Victorian MP's pay, it is nonetheless incumbent upon the VIRT to consider the fact that women MPs are more likely to enter the parliament already having suffered financial disadvantage through the superannuation system.

Women MPs entering parliament will be broadly reflective of the community in terms of their superannuation balances when you consider the following factors that driving this inequality, including:

- the undervaluing of industries and occupations dominated by women;
- the gender pay gap; and
- the breaks in career & superannuation contributions that women experience over a lifetime of work due to their caring responsibilities

Women MPs are more likely (but not exclusively) to be in the cohort of MPs ineligible for the defined benefits scheme, further entrenching the gender gap in retirement income.

Any inequities or irregularities identified by the PWC actuarial modelling in the two schemes for women elected/appointed to the Victorian parliament from 2004 would further exacerbate their pre-existing superannuation disadvantage.

Recognition of prior service

Across the public sector it is common practice for employees to have prior service recognised, this generally includes long service leave, annual leave, sick leave and other commonplace entitlements.

This principle should also be considered by the VIRT for superannuation purposes for MPs, whether this be prior service with the Victorian parliament or other jurisdictions such as the commonwealth parliament.

Submission responses to VIRT's issues paper questions for consideration

- i. *Analytical framework: Is the Tribunal's proposed analytical framework for identifying potential inequalities and irregularities, and for considering options to address these, appropriate and complete? If not, why?*

Broadly speaking, the Tribunal's proposed analytical framework is appropriate to assist in the identification of potential inequalities and irregularities.

It will be important for the Tribunal to ensure that the actuarial modelling is sufficiently broad to capture a relative cross-section of the MPs experiences rather than to limit them to simply an average age at which MPs entered Parliament or their average length of service.

When a similar review was undertaken by the Independent Parliamentary Standards Authority (IPSA) in the UK, they undertook analysis across the following sub-groups for comparing superannuation benefits:

- Younger age and shorter tenure
- Older aged and shorter tenure
- Medium stayer
- Longer stayer

To ensure the Tribunal's analysis appropriately considers the broad spectrum of MPs personal circumstances, a similar approach to the above would appear to provide more relevant and meaningful analysis than the *average* experience. The age and tenure for each grouping should reflect the experience of Victorian MP career data the VIRT has access to.

Other feedback about the key elements of the VIRT's analytical framework are addressed throughout the remainder of this submission.

- ii. *Comparing schemes: How (if at all) should the Tribunal compare the outcomes for MPs who are members of the defined benefit schemes and the Accumulation Scheme respectively? For example, is the Tribunal's proposed actuarial modelling approach, outlined in section 5, appropriate? Moreover, is the Tribunal's proposal to focus on a comparison of the accumulation and New Benefits schemes appropriate? If not, why?*

Focus on New Benefits Scheme and Accumulation Scheme

The Tribunal notes that it intends to focus its review on the New Benefits Scheme and the Accumulation Scheme which seems entirely reasonable given there are no current MPs who are in the Existing Benefits Scheme and the reasons for closing that scheme to new members was markedly different than that which occurred in 2004.

Principle of horizontal equity is most relevant

The Tribunal notes the principle of horizontal equity appears to be the most relevant for this review. The VIRT is seeking to compare the outcomes between MPs from one scheme to another where the only discernable difference has nothing to do with the work they perform, but whether they were employed one day before the New Benefits Scheme closed to new members or one day after.

Notwithstanding the limitations of how this principle may be applied to address any inequitable outcomes, the VIRT's report should ensure it documents the full extent to which such inequities exist.

Proposed actuarial modelling

The Tribunal has proposed to undertake a *backward-looking approach* to compare the benefits an MP would have had if they joined the Accumulation Scheme in 2004, compared to the benefit they would have received as a member of the New Benefits Scheme for the same period.

It has also proposed a *forward looking approach* to forecast the total superannuation benefits provided to an MP joining the Accumulation Scheme in 2020 and serving a given number of years compared to the superannuation benefit they would have received had they instead been a member of the New Benefits Scheme for those years.

This is perhaps the most important aspect of this review because it will demonstrate the variability of MPs retirement outcomes between the two schemes. Such analysis will be an integral element to support any VIRT recommendations to Government in its final report.

It is assumed that the VIRT will provision actuarial modelling and the assumptions and calculations performed will be appropriate, applied consistently and documented for transparency.

Important considerations in this regard will include but not be limited to:

- How the difference between the outcomes between the two schemes will be demonstrated. Presumably the most easily understood approach will be to convert benefits to a lump sum after tax equivalent calculation in today's dollars.
- The method by which any reversionary benefits will be valued and included in the calculation to compare the entirety of the different benefits available between the two schemes
- How the separation payment for MPs in the Accumulation Scheme is incorporated into the modelling
- The rate of indexation applied to key data elements such as salaries, contributions, pension payments and where these differ between the schemes (and to the extent applicable, the reasons why and the impact of those differences)
- The rate of concessional and non-concessional contributions assumed or not assumed to be made to each scheme (and where these differ the reasons why and the impact of those differences). In this regard it is important to note that while the New Benefits Scheme generally requires an 11.5% voluntary contribution from MPs, no such contribution is required from MPs in the Accumulation Scheme, but if an accumulation member was to make the same level of contribution, they are bearing the whole of the investment risk on those monies which is significantly different to members of the New Benefits Scheme.
- Any difference in tax treatment between the contributions made to the respective schemes (the most relevant issues appear to be noted in the VIRT's issue paper already)
- The investment options/earnings rates used relative to the accrual and benefits paid from the respective schemes
- Any difference in tax treatment on payment from the schemes or income and assets assessed on draw-down of a pension benefit from the schemes.

Depending on the Victorian MP data analysed and the degree to which different benefit payment types are statistically significant in the data, it may be appropriate to include a comparison of the different outcomes between the two schemes upon death, disability or ill-health payment conditions being met in addition to standard payment types such as resignation and retirement benefits. This may include the need to incorporate the default insurance cover arrangements of the Accumulation Scheme to consider how MPs in the Accumulation Scheme are protected compared to those in the New Benefits Scheme.

iii. Inequalities: What inequalities should the Tribunal consider? Has the Tribunal identified the main inequalities in this paper? What reforms are needed to address these inequalities? What factors should the Tribunal take into account when considering potential changes?

Based on the previous recommendations of the Hazell review, it is anticipated that the key inequality identified by the Tribunal will be the extent to which the Accumulation Scheme benefits produces an inferior outcome when compared to the New Benefits Scheme.

While the separation payment may go some way to addressing this gap, it is likely that the longer the period of tenure the greater the disparity becomes.

Given the Tribunal is unable to consider options that would negatively impact existing or former MPs benefits, it would seem there are a limited range of options:

- Make no recommendations and let the inequities remain
- Make recommendations that seek to artificially address any differences by making changes to the Accumulation Scheme or other entitlements provided to MPs to make them comparative to the New Benefits Scheme outcomes (similar to what the Hazell Review attempted to do)
- Make recommendations that seek to fully address and remove such disparities (for example, reopening the New Benefits Scheme).

Unless the actuarial modelling indicates that the differences between the scheme are minor in the context of an MP's remuneration and retirement savings outcomes, it is difficult to see how the Tribunal could be satisfied to let material inequities remain regardless of:

- the environment the Government was operating in when the decision to close the New Benefits Scheme was made; or
- the extent to which past efforts to address identified differences has been tempered by a desire to balance community expectations against the direct personal financial detriment that has befallen current MPs attached to the Accumulation Scheme.

iv. Irregularities: What irregularities should the Tribunal consider? Has the Tribunal identified the main irregularities in this paper? What reforms are needed to address these irregularities? What factors should the Tribunal take into account when considering potential changes?

The most notable irregularity as noted in the Tribunal's issues paper is that pertaining to the different tax treatment between defined benefits and Accumulation Schemes, particularly in the area of contributions.

Grandfathering and concessional contributions

While New Benefits Scheme members benefits are essentially protected from any adverse impact of concessional contributions caps, MPs contributing to the Accumulation Scheme are not. This may result in an irregularity where the Victorian Government's compulsory contributions to the Accumulation Scheme alone (or inclusive of any salary sacrifice contributions paid by the MP) results in MPs exceeding their concessional contributions cap and thus excess contributions being included in their assessable income and subject to their marginal rate of tax.

This is likely to manifest itself as an issue in the calculations comparing the two schemes outcomes and will need to be dealt with in the assumptions of that work.

A further difference as touched on earlier in the paper is the significant difference between who assumes the investment risk between a defined benefit plan and an accumulation plan. While it may be necessary to model the respective benefits of each plan assuming a similar level of personal contributions from MPs to each plan, it is important to consider that MPs making those contributions to an Accumulation plan are not protected from market losses on those in the same way as a member of the New Benefits Scheme. Accordingly, it may be impractical to expect that contributions at that rate would actually occur in practice and even if they did, it may be prudent or appropriate to consider that the investment returns on those is more conservative than aggressive.

- v. *Commonwealth legislation: What is the impact of Commonwealth legislation on Victorian MP superannuation schemes, and what options should the Tribunal consider to address these impacts?*

It may be relevant to consider the different tax treatment on end benefits from each scheme including how the benefit will be calculated in accordance with the Australian Taxation Office's Transfer Balance Cap.

Defined benefit pensions may be subject to special rules that effectively discount their value when compared to lump sum benefits transferred from an Accumulation Scheme to an account-based pension scheme for example. This difference may present as an issue in the calculations comparing the two schemes outcomes and will need to be dealt with in the assumptions of that work.