Chapter summary

The Committee examined offsetting arrangements between the Veterans’ Entitlements Act 1986 (VEA) and the Safety, Rehabilitation and Compensation Act 1988 (SRCA). This matter has been the subject of widespread criticism and concern in the veterans’ community for some years.

Offsetting occurs because certain claimants have dual eligibility and are able to claim compensation under both the VEA (pension) and the SRCA (permanent impairment lump sum payments and incapacity payments). Dual eligibility dates from 1972, when Australian Defence Force (ADF) members on peacetime service became eligible to claim under the two compensation schemes. The enactment of the Military Rehabilitation and Compensation Act 2004 (MRCA) from 1 July 2004 ceased the practice of dual eligibility for all forms of service from that date. However, dual eligibility continues for service before 1 July 2004. A key principle of offsetting is that dual eligibility should not result in claimants receiving benefits greater in value than the more generous of the benefits available under either the SRCA or the VEA for the same incapacity or death.

Out of 120,755 disability pensioners (as at September 2010), almost 9,000, or 7 per cent have their disability pension offset. In addition, 370 war widow(er)s have had their war widow(er)’s pension offset. The average disability pension offset is approximately $87.00 per fortnight. The average war widow(er)’s pension offset is approximately $313.00 per fortnight. These total approximately $25 million per year.

Offsetting is the process of reducing one compensation payment in recognition of another compensation payment for the same incapacity or death, so that a claimant does not receive double compensation. Offsetting typically occurs when a claimant receives a pension under the VEA and subsequently elects to receive a SRCA lump sum payment for the same incapacity or death. The legislation that governs the offsetting arrangements requires that the lump sum be converted to give a fortnightly payment equivalent. This conversion uses factors provided by the Australian Government Actuary, which take account of the claimant’s age. The fortnightly VEA pension is then reduced for the life of the claimant by an amount initially equal to the fortnightly equivalent (this amount increases in line with the Consumer Price Index).

Submissions to the Review did not take issue with the principle underlying offsetting, but were critical of the methodology. Claimants argue that offsetting should cease once the original amount has been repaid or, alternatively, upon claimants attaining their actuarial age. In 2003, these issues were the subject of a specific inquiry by the Senate Foreign Affairs, Defence and Trade Legislation Committee. The Senate Committee did not recommend changing the offsetting arrangements, noting that the introduction of the MRCA would cease dual eligibility for future service and thus the problem would eventually cease to exist.

The Committee examined the current actuarial model used for the offsetting calculation and three alternatives: a modified actuarial model; a loan model; and ceasing the offset when the lump sum is ‘paid back’. Any changes to existing military compensation offsetting arrangements would need to be considered from a whole-of-government
perspective, since offsetting calculations based on an actuarial model are not confined to military compensation.

In the actuarial model, the total dollar amount offset against a claimant’s pension over his or her lifetime usually exceeds the lump sum amount. This feature can result in perceived inequities. However, on average, the cost to the Commonwealth of providing the lump sum benefits is equal in value to the savings arising by offsetting the pensions.

To remain cost neutral to the Commonwealth, the modified actuarial model would result in a higher offset than the current approach, but the offset would cease when claimants reach their actuarial age (life expectancy). However, the higher offset would be unlikely to gain claimants’ support.

In the loan model, when the offsetting process commences, the relevant part of the pension would be set to zero (fully offset); and when the loan is fully repaid, including an appropriate allowance for interest, the disability pension would be restored to full value for the rest of the claimant’s life. The loan model would cost the Commonwealth 5–10 per cent more than the actuarial model. In addition, the 2003 Senate Inquiry concluded there were too many complexities associated with this model.

By ceasing the offset when the lump sum is ‘paid back’, the offset effectively becomes a non-interest loan. This approach has the benefit of being simple to understand, but it violates the key principle of offsetting mentioned earlier. Since this approach ignores the time value of money, claimants with dual eligibility would be able to receive benefits of greater value than under either the SRCA or VEA individually.

The Committee believes that these alternative models are complex and not cost effective, and recommends that existing offsetting arrangements be maintained. The Committee also recommends that the Repatriation Commission further explore the concept of giving claimants a choice, at the date any offset is determined under the VEA, to pay back the actuarial value of the lump sum previously received under the SRCA.

Since the complexities of the current offsetting arrangements make information difficult for many claimants to fully understand, it is important that the advice given to potential claimants is comprehensive, accurate and clear. The Committee recommends that the Department of Veterans’ Affairs continue its efforts to improve advice to clients regarding the effect that offsetting provisions will have on their compensation entitlements.

**Introduction**

19.1 This chapter addresses offsetting arrangements between the *Veterans’ Entitlements Act 1986* (VEA) and the *Safety, Rehabilitation and Compensation Act 1988* (SRCA), a matter that has been the subject of widespread criticism and deep concern in the veteran community for some years.

19.2 While submissions to the Review did not take issue with the principle underlying offsetting, they were critical of the methodology. Claimants argue that offsetting should cease once the original amount has been repaid or upon claimants attaining their actuarial age (life expectancy).

19.3 Other offsetting issues, such as offsetting incapacity payments against superannuation pensions and offsetting in relation to transitional permanent impairment calculations, are dealt with elsewhere in this report.

19.4 In this chapter, the term ‘claimant’ is used generically to cover a range of terms, including veteran, member, former member, widow(er) and dependent partner.
Offsetting refers to the process of reducing one compensation payment in recognition of another compensation payment for the same incapacity or death. This upholds the principle that a claimant with dual eligibility should not receive compensation of greater value than is available under either the SRCA or VEA individually. Where a claim is made under both the VEA and the SRCA for an incapacity arising from the same injury or illness, offsetting of benefits occurs.

Typically, a claimant receives a pension under the VEA and subsequently elects to receive a SRCA lump sum payment for the same injury, illness or death. However, it is not unusual for the reverse to occur, where the claimant receives a lump sum payment and subsequently receives a VEA pension for the same injury, illness or death.

Comparisons between VEA and SRCA entitlements are complex because of the different nature of payments. The VEA provides fortnightly payments, and SRCA permanent impairment compensation is paid as a lump sum.

To make the amounts comparable and enable them to be offset, the lump sum is converted using actuarial tables to determine a fortnightly payment equivalent. The pension is then reduced accordingly, and the reduction is for the life of the claimant.

The actuarial tables are prepared by the Australian Government Actuary. They take into account the claimant’s age, and thus the prospective payment period. The fortnightly VEA pension is reduced for the life of the claimant by an amount initially equal to the fortnightly equivalent determined using the actuarial tables, which subsequently increases in line with the Consumer Price Index (CPI).

It is worth emphasising that this category of offsetting occurs because, and only because, certain claimants have dual eligibility (the ability to claim compensation under both the VEA and the SRCA).

This dual eligibility dates back to 1972, when Australian Defence Force (ADF) members on peacetime service became eligible to claim under the two separate compensation schemes. At the same time, the Compensation (Commonwealth Government Employees) Act 1971 continued to cover peacetime service. ADF members were not entitled to receive benefits under both Acts for the same injury or illness. However, they could elect to receive the benefit most beneficial to them. As noted earlier, a key principle of offsetting is that dual eligibility should not result in claimants receiving benefits greater in value than the more generous of the benefits available under either the SRCA or the VEA individually, for the same incapacity.

Justice Toose’s comments (made in 1975) on this subject are prophetic:

There has been strong criticism that there should exist two separate compensation schemes for members of the Forces providing cover in respect of the same

2 ibid., p. 59.
employment situation. Evidence has been presented that indicates that members have great difficulty understanding the present relationship between the two schemes and in determining the legislation under which to claim.

19.13 The foregoing criticism fails to mention that dual eligibility effectively advantaged claimants with peacetime service over those with operational service.

19.14 This situation was maintained for more than 20 years. On 7 April 1994, the Military Compensation Act 1994 extended the operation of the SRCA (and therefore dual eligibility) to operational service. At the same time, dual eligibility ceased for those who enlisted on or after 22 May 1986 (the date the VEA came into operation) and were injured on peacetime service after the introduction of the Military Compensation Act. Coverage for this group is under the SRCA only.

19.15 The enactment of the Military Rehabilitation and Compensation Act 2004 (MRCA) on 1 July 2004 ceased the practice of dual eligibility under the VEA and the SRCA for all forms of service from that date. However, dual eligibility under the VEA and the SRCA does continue for service before 1 July 2004.

**Benefits and inequities of dual eligibility**

19.16 Even though offsetting is designed to ensure that no one receives a benefit of greater (actuarial) value than under either SRCA or VEA individually, the simple fact that people with dual eligibility are able to receive both pension and lump sum benefits provides them with some advantage.

19.17 In a major inquiry into military compensation during the 1990s, it was argued that dual eligibility has effectively created a third compensation scheme.\(^3\) A subsequent review found the ‘outcomes to be over generous compared to those available to members of the veteran community without dual eligibility’.\(^4\)

19.18 Dual eligibility also means that claimants involved in the same accident may be entitled to different compensation benefits, because some will have dual eligibility and some will not. This problem was brought into sharp focus following the crash of two Black Hawk helicopters in June 1996, causing a fundamental reappraisal of military compensation arrangements that eventually led to the removal of dual eligibility. The HMAS *Westralia* accident two years later similarly highlighted this issue.

19.19 Dual eligibility continues to be a key source of complexity, confusion and misunderstanding among administrators, claimants and their representatives. It was a central reason for the development and enactment of the MRCA as a single piece of compensation legislation covering all forms of service.

**Offsetting figures**

19.20 Out of 120,755 disability pensioners (as at September 2010), almost 9,000, or 7 per cent have their disability pension offset. In addition 370 war widow(er)s have had their war widow(er)’s pension offset. The average disability pension offset is approximately $87.00 per fortnight. The average war widow(er)’s pension offset is approximately $313.00 per fortnight. These total approximately $25 million per year.

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19.21 It is difficult to estimate the total number of claimants who would qualify for
dual eligibility for both peacetime and operational service. In 1997, the Inquiry into
Military Compensation Arrangements ‘estimated that there are approximately 210,000
former and serving members of the ADF that have eligibility for dual entitlements’. 5

2003 Senate Inquiry into offsetting between the Veterans’ Entitlements
Act and the Safety, Rehabilitation and Compensation Act

19.22 In 2003, offsetting between the VEA and the SRCA was the subject of a
specific inquiry by the Senate Foreign Affairs, Defence and Trade Legislation
Committee — ‘Aspects of the Veterans’ Entitlements Act 1986 and the Military
Compensation and Rehabilitation Scheme’. This inquiry stemmed from complaints by
ex-service organisations (ESOs) and individuals about offsetting methodology issues.
The tenor of those complaints has been repeated in the submissions to this Review.

19.23 After examining the rationale and methodology relating to offsetting, as well as
being exposed to an alternative model (the loan model, explained later in this chapter)
the Senate Committee concluded that it was ‘not able to make any recommendations in
favour of those recipients who are currently affected by the offsetting arrangements’. 6

19.24 In short, the Senate Committee did not recommend moving away from the
offsetting arrangements that existed then and continue today (the actuarial model). It
acknowledged that to do so would have resulted in additional costs to the
Commonwealth.

19.25 The Senate Committee confined its recommendations to the need for the
Department of Veterans’ Affairs (DVA) to provide more helpful information to
claimants. It was noted at the time that the impending introduction of the MRCA would
cease dual eligibility for future service, thus the problem would eventually go away. 7

Nature of complaints about offsetting arrangements

19.26 Complaints about offsetting arrangements revolve around three issues. First,
that claimants were not made aware, or were not made aware to the extent they should
have been, that their VEA pensions would be reduced for the rest of their life. 8

19.27 Claimants argue they either assumed or were advised that their pension would
be reduced only for the time it took to ‘repay’ the lump sum payment they had received.
That is, that their pension would be reduced for a period until the reduction amount
equalled the lump sum they had received.

19.28 Second, some claimants argue that they, or someone they know, have ‘paid’ in
excess of the lump sum payment they received. Almost invariably, this involves
claimants who received the lump sum at a relatively young age and who are
approaching, or who have lived beyond, their actuarial age. Claimants are aware that if
they die before their life expectancy, no recovery is made against their estate if the lump
sum has not been repaid on a nominal dollar basis (without allowing for interest).

5 P Gourley, op. cit., p. 16.
6 Senate Foreign Affairs, Defence and Trade Legislation Committee, Inquiry into aspects of the Veterans’
Entitlements Act 1986 and the Military Compensation and Rehabilitation Scheme, Senate Foreign Affairs,
7 ibid., p. 27
8 See, for example, the submission to the Review by Mr A Wheatley.
Third, complaints arise about the fact that the offset amount is indexed. This, according to the Actuary, followed a High Court decision in the 1980s relating to discounting of compensation awards.9

With respect to the first point, there is no question that the advice given to potential claimants needs to be comprehensive, accurate and clear. It also needs to be provided in sufficient time for the claimant to make an informed decision about whether or not to claim the lump sum (or pension). It is also clear that the complexities of the offsetting arrangements make this information difficult for many claimants to fully understand.

Currently, before a determination for SRCA lump sum compensation, an election form is sent to an eligible claimant offering him or her a choice to accept the payment. The covering letter notifies the claimant that:

• if he or she decides to accept the lump sum, it could also affect any disability pension;
• if he or she is in receipt of a disability pension, the estimated effect of the lump sum on that pension is quoted;
• if the rate of disability pension is varied in the future, the reduction as a result of the lump sum may also be varied; and
• the offset will be applied for the duration the claimant is in receipt of the disability pension, usually for life.

The claimant is asked to complete and return the election form within 21 days, advising their decision about receiving SRCA compensation. If the lump sum payment would affect an existing disability pension, no further action is taken until an election is made by the claimant. If payment of the lump sum would not affect any disability pension and an election is not made within 21 days, the lump sum is paid.

This practice provides the claimant with information and ensures that the payment of SRCA compensation does not lock the claimant into lifelong offsetting of their existing disability pension.

The second, and more fundamental, aspect of the complaints about offsetting contends that the reduced rate of pension should be returned to its former level once claimants reach their actuarial age or, alternatively, when the lump sum (plus some amount of unspecified interest) has been repaid. This arises from a fundamental confusion over the purpose of the offset, and the mistaken belief that it is a kind of loan, as opposed to a reduction in payment recognising the fact that the same incapacity or death should not be compensated more than once.

This leads to a discussion about the manner in which the lump sum is offset (the actuarial model) and, in turn, the question of whether there are any viable alternatives to that model. Following is an analysis of the current actuarial model and consideration of three alternatives:

• a modified actuarial model;
• the loan model; and
• ceasing offset when lump sum is ‘paid back’.


264 Review of Military Compensation Arrangements
The actuarial model

19.36 Under the actuarial model, the disability pension is reduced by an amount that is actuarially equivalent to the lump sum. In the case of a very large lump sum, the pension may be fully offset (i.e. no disability pension or war widow(er)’s pension is payable).

19.37 The actuarial model is prospective in nature. That is, for any claimant, at the time the offsetting process begins, the actuarial present value of future offset amounts equals the value of the lump sum that is being offset. In the words of the Actuary: 10

A natural consequence of the actuarial model is that this valuation equivalence does not hold after commencement. The assumptions underpinning the actuarial model (both demographic and economic) will not be exactly borne out in practice for an individual. Therefore, the actual (after death) hindsight value of the offsets in any individual case will be different from the lump sum. This feature of the model is not a flaw, but it has led to perceived inequities. [Emphasis added]

19.38 In essence, the Actuary is using the same principles that underpin lifetime annuities. A life insurance company will pay an annuity for life, in exchange for an up-front lump sum premium. The amount of the periodic annuity depends on certain assumptions, particularly the life expectancy of the person and the rate of interest to be earned on the invested lump sum.

19.39 Importantly, because the life insurance company has the opportunity to invest the lump sum and earn interest on it, the total of annuity payments over the lifetime of the person is expected to be more than the initial lump sum premium. Similarly, the total dollar amount offset against a claimant’s disability pension over his or her lifetime is expected to exceed the lump sum amount.

19.40 The compensation offsetting model is designed to ensure that each claimant has access to both the SRCA and VEA, and gets a benefit equal in value to the greater of the benefits available under either scheme individually, while resulting in no substantial net loss or gain for the Australian Government. The demographic and economic assumptions underpinning the model apply to the cohort as a whole and will not be borne out in practice for each individual. Some claimants will die before their actuarial age, others after.

19.41 The Actuary notes that, in any individual case, the actual (after death) value of the offset will be different from the lump sum. This leads to a perception of inequity by claimants who, not surprisingly, are looking at the matter through the prism of individual cases, rather than from the perspective of how the overall system functions.

19.42 Perceptions of inequity have given rise to arguments that offsetting should cease when claimants reach their actuarial age. Essentially, this is the point at which the initial outlay becomes cost neutral to the Australian Government for that individual. From the claimant’s perspective, this is the age where the original lump sum might be considered to have been ‘repaid’.

19.43 However, the opposite situation arises where a claimant dies before reaching their actuarial age. In this case, the Australian Government has paid more in lump sum compensation to that claimant than would ordinarily have been paid had they chosen to receive only the original pension.

19.44 Claimants who live beyond their actuarial age are, in effect, ‘underwriting’ those claimants who die before their actuarial age. This is entirely consistent with the model, given that it is designed to be cost neutral to the Australian Government. As the Senate Inquiry noted in September 2003: 11

… the actuarial model is designed to deliver the better of two possible benefits to the veteran or widow. The Tables in the Actuary’s instructions are calculated to ensure, that overall, the figures will average out over time for most recipients.

First alternative: the modified actuarial model

19.45 The Actuary has developed an alternative model that may be described as the modified actuarial model. This model would:

• result in overall cost neutrality for the Australian Government;
• result in an initially higher offset; but
• allow offsetting to cease when claimants reach their actuarial age.

19.46 The current actuarial model calculates a fortnightly offset by using factors based on lifetime annuity values. In contrast, the modified actuarial model would use factors based on contingent life expectancy annuity values. This would result in a higher offset designed to cease when claimants reach their actuarial age, while taking into account that a certain proportion of claimants will die before they reach their actuarial age.

19.47 While the modified actuarial model is cost neutral for the Australian Government and allows offsetting to cease at actuarial age, it necessitates a higher offset amount, making support by claimants unlikely. It is also probable that this model could only be implemented prospectively, as it would be very complex and difficult to do so retrospectively. It would also involve cost increases associated with upgrading DVA systems.

19.48 The Actuary has advised the Review that he could modify the model further to eliminate indexing the offset amount. He explained the effect of this would be that the offset would, in real terms, be a larger amount in the early stages and a smaller amount in the later stages.

19.49 The Actuary pointed out that indexing the offset by the CPI uses factors based on real interest rates, which are more stable than nominal interest rates. In introducing a non-indexed offset, it would be necessary to take into account movements in nominal interest rates, and this would require adjusting the actuarial factors more frequently (perhaps every two or three years).

Example

19.50 Under the current actuarial model, a 40-year-old male who receives a $10,000 lump sum would have his disability pension reduced by $17.05 per fortnight. The reduction would increase over time in line with the CPI. This arrangement would continue for the rest of his life.

19.51 Under the modified actuarial model, a 40-year-old male who receives a $10,000 lump sum would have his disability pension reduced by $18.23 per fortnight. The

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11 Senate Foreign Affairs, Defence and Trade Legislation Committee, op. cit. p. 25.
reduction would increase over time in line with the CPI until the claimant reached age 79, when the offset would cease.

Second alternative: the loan model

19.52 In the context of the 2003 Senate Inquiry, the Actuary was asked to provide a formulation for a ‘loan model’ with the aim of seeking to address concerns raised about the actuarial model. The Actuary has provided the following formulation of a loan model:

- at the time the offsetting process commences, the relevant part of the disability pension is set to zero (fully offset); and
- when the loan is fully repaid, including an appropriate allowance for interest, the disability pension is restored to full value for the rest of the claimant’s life.

19.53 The current actuarial model works on a prospective basis (that is, it works on the basis of assumptions made at the time payment commences). The loan model works on a retrospective basis (that is, assumptions are adjusted over time as the lump sum is repaid, with interest).

19.54 The Actuary estimates that the loan model would cost the Australian Government 5–10 per cent more than the actuarial model if the same interest rate basis is used for both, before taking into account higher administrative costs. This is because in cases where the claimant dies before their actuarial age, the offset would be less than the lump sum amount. However, in cases where a claimant outlives their actuarial age, offsetting does not continue.

19.55 If the loan model were varied to incorporate partial offsetting instead of full offsetting until repayment, the cost to the Australian Government would be higher (assuming no recovery from estates). That is because, in more cases, less of the ‘loan’ would be recovered before the death of the claimant.

19.56 To achieve a loan model that is of no cost to the Australian Government, a complex and probably unpopular recovery system would be needed. Under such a recovery system, the Australian Government would need to recover unpaid amounts from estates in cases of premature death. Such a model would be difficult to design, cumbersome to administer, and would be highly unpopular in relation to those cases where recoveries were required (an estimated 25 per cent of cases).

19.57 The feasibility of the loan model was considered by the 2003 Senate Inquiry. It concluded there were simply too many complexities associated with this approach. This included dealing with calculations for ‘loans’ of varying lengths and the need to calculate and administer fluctuating interest rates, which would involve varying pension deduction rates, in some cases substantially, as a consequence of changes in interest rates.

19.58 The Senate Inquiry also noted that DVA’s information technology systems would need to be substantially upgraded to accommodate such a system, with a related increase in administrative costs. This remains a factor to consider today.
Third alternative: cease offsetting when lump sum is paid back dollar for dollar

19.59 The financial concepts on which offsetting is premised, such as the time value of money, are not well understood by many beneficiaries under the VEA. Several submissions contend that the offset should cease when the amount repaid is equivalent, dollar-for-dollar, to the original lump sum, equating the offset to the repayment of a (non-interest) bank loan.

19.60 Ceasing the offset when the total offset equals the lump sum amount has the benefit of being simple to understand. However, it inflates the benefit of choosing a lump sum over a pension. Since it ignores the time value of money, it violates a key principle of offsetting, as claimants with dual eligibility would be able to receive benefits of greater value than under the VEA or SRCA individually.

19.61 Further complications arise where a claimant’s offset has been in place for a long time. In those instances, the total dollar amount of the offset is likely to exceed the dollar amount of the original lump sum. The effect of this is that DVA would be required to repay offset amounts exceeding the lump sum. This option has a significantly greater cost to the government than the loan model.

Determining how much has been ‘repaid’

19.62 Claimants argue that many individuals have ‘repaid’ far more than the original lump sum they received. It is also based on comparisons of historical lump sum amounts with current offset amounts, and does not take into account the changing value of the amounts, or any consideration of interest.

19.63 The figures set out in Table 19.1 have been supplied by the Actuary. They compare the accumulated value of offsets with the present value (as at June 2010) of a $1,000 lump sum across a range of ages and commencement dates. (The accumulation factor used is the long-term bond rate.)

<table>
<thead>
<tr>
<th>Age at lump sum</th>
<th>1975 ($)</th>
<th>1980 ($)</th>
<th>1985 ($)</th>
<th>1990 ($)</th>
<th>1995 ($)</th>
<th>2000 ($)</th>
<th>2005 ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>30</td>
<td>9,939</td>
<td>12,288</td>
<td>4,764</td>
<td>2,166</td>
<td>1,226</td>
<td>679</td>
<td>263</td>
</tr>
<tr>
<td>40</td>
<td>11,459</td>
<td>13,055</td>
<td>5,492</td>
<td>2,475</td>
<td>1,390</td>
<td>764</td>
<td>293</td>
</tr>
<tr>
<td>50</td>
<td>14,049</td>
<td>14,632</td>
<td>6,734</td>
<td>3,011</td>
<td>1,674</td>
<td>911</td>
<td>342</td>
</tr>
<tr>
<td>60</td>
<td>18,629</td>
<td>17,693</td>
<td>8,929</td>
<td>3,961</td>
<td>2,184</td>
<td>1,178</td>
<td>431</td>
</tr>
<tr>
<td>Present value of lump sum</td>
<td>24,064</td>
<td>15,079</td>
<td>7,845</td>
<td>4,269</td>
<td>2,642</td>
<td>1,850</td>
<td>1,397</td>
</tr>
</tbody>
</table>

19.64 While it is difficult to determine exactly how many individual cases are involved, the Actuary’s findings do not sustain the claims made that there are many cases where the original lump sum awarded had been ‘more than paid off’. The table shows that by June 2010, only two of the 28 illustrative groups of disability pensioners
have pension offsets that have accumulated to more than the present value of the lump sum.\textsuperscript{12}

**Examples**

19.65 A $1,000 lump sum paid in 1975 and invested at the long-term bond rate would have a value of $24,064 in 2010. A claimant who was 30 at the time the lump sum was paid would have ‘paid back’ an accumulated value of $9,939 in offsets against his or her disability pension.

19.66 A $1,000 lump sum paid in 1990 and invested at the long-term bond rate would have a value of $4,269 in 2010. A claimant who was 40 at the time the lump sum was paid would have ‘paid back’ an accumulated value of $2,475 in offsets against his or her disability pension.

**Assessing the value of the lump sum**

19.67 It is not widely understood by those arguing about offset ‘repayment’ that $1,000 invested at the long-term bond rate in 1975 would have grown to $24,064 by 2010. Thus, claimants may not have taken sufficient account of what their lump sum would have been worth had they invested it (particularly in a high interest rate environment, such as in the 1980s) or, alternatively, used it to pay off debt.

19.68 As the Actuary pointed out in his report to the Senate Inquiry in 2003, claimants who had the use of lump sums in the late 1970s and throughout the 1980s benefited from the high interest rates of that period to a greater degree than they probably realise.\textsuperscript{13}

19.69 It is likely that the present value of lump sums is not given sufficient weight in comparisons between lump sums and the amount offset from pensions over time.

**Broader application of actuarial offsetting**

19.70 Offsetting calculations based on the actuarial model are not confined to military compensation. For example, payment of a superannuation surcharge debt (upon retirement) for an Australian Government superannuation scheme may be affected by reducing the pension on an actuarial basis. Hence, any changes to existing military compensation offsetting arrangements would need to be considered from a whole-of-government perspective.

19.71 It is worth noting that the fact sheets provided by the four superannuation schemes,\textsuperscript{14} which explain the mechanism for paying the surcharge debt by reducing the relevant scheme pension, do not state explicitly that, should such an option be chosen, the pension will be reduced for the recipient’s life.

\textsuperscript{12} For disability pensioners who were aged 60 in 1980 and in 1985, and who were still alive in 2010, the value of their respective accumulated pension offset ‘repayments’ in 2010 was $17,693, compared with a present value of the $1,000 lump sum of $15,079, and accumulated pension offset ‘repayments’ of $8,929 compared with the present value of the $1,000 lump sum of $7,845.

\textsuperscript{13} Australian Government Actuary, op. cit., p. 10.

\textsuperscript{14} Commonwealth Superannuation Scheme; Public Sector Superannuation Scheme; Military Superannuation and Benefits Scheme; Defence Force Retirement and Death Benefits Scheme.
Repaying the lump sum at the date the offset is calculated

19.72 The Committee considered whether a VEA claimant who has previously received a lump sum under the SRCA, which would be offset against a VEA pension, could be provided with a choice at the date the pension offset is calculated to repay the actuarial value of the lump sum in order to maximise the pension payable.

19.73 Currently, if a beneficiary is receiving a pension under the VEA, they may choose (if eligible) to receive a lump sum under the SRCA and have their pension offset. Conversely, they may choose not to receive a lump sum under the SRCA and continue to receive a full pension under the VEA.

19.74 However, some claimants may have been paid a lump sum under the SRCA, without being aware at that time of their potential eligibility for a pension under the VEA. In fact, it may be years later that some claimants become aware of their VEA eligibility.

19.75 In these circumstances, the claimant has lost the choice to take a full pension in lieu of a lump sum. DVA is endeavouring to ensure that claimants are aware of their potential eligibility under all of the legislation it administers, but it is inevitable that this will continue to occur in some cases.

19.76 Although the proposal appears to be straightforward, the Actuary has identified some complexities in its implementation. If these complexities could be addressed, while maintaining simplicity for beneficiaries, the Committee supports the provision of a choice for those in this situation.

Conclusions

19.77 There are strong grounds for maintaining the status quo:

- the existing offsetting arrangements are designed to provide claimants with an enhanced compensation benefit — a pension and a lump sum — resulting from being able to claim compensation under two separate pieces of legislation, while still being cost neutral to the Australian Government;

- complaints about offsetting ignore, or appear not to give sufficient weight to, the actual present value of the original lump sum payments;

- the number of cases involving recipients who have already had their pensions offset by more than the value of their lump sum after allowing for a reasonable rate of interest, appears to be less than claimed, perhaps considerably less, in the light of the analysis undertaken by the Actuary;

- the current offsetting method takes into account that some claimants will die before their actuarial age; and

- offsetting arrangements based on actuarial calculations are not confined to military compensation; they are also used for superannuation pension reductions designed to repay a superannuation surcharge debt. Hence, any proposed changes to existing offsetting arrangements would need to be considered from a whole-of-government perspective.

19.78 The other models discussed in this chapter are complex and not cost effective.

19.79 The Committee appreciates the concerns raised by claimants, and acknowledges the confusion that offsetting calculations can cause. However, on balance, the
Committee favours continuation of the existing actuarial offsetting arrangements under the VEA.

19.80 Should government wish to change the existing arrangements, the Committee considers the most viable to be the model based on offsetting ceasing at actuarial age (the modified actuarial model).

19.81 Lastly, the Committee believes that the viability of providing claimants with the option to pay back the actuarial value of a lump sum previously received under the SRCA at the time an offset to a pension is determined under the VEA should be examined by DVA, in association with the Actuary. This should only be pursued if it provides choice to claimants and relative simplicity.

**Recommendations**

The Committee recommends that:

19.1 existing offsetting arrangements be maintained;

19.2 ongoing efforts by the Department of Veterans’ Affairs (DVA) aimed at improving advice to clients regarding the effect offsetting provisions will have on their compensation entitlements be continued; and

19.3 DVA should examine the viability of providing claimants with the option to repay the actuarial value of a lump sum previously received under the *Safety, Rehabilitation and Compensation Act 1988* at the time an offset of a pension is determined under the *Veterans’ Entitlements Act 1988*, taking into account the benefits of increased flexibility while maintaining simplicity.