Monday, 23 January 2023

Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Via website

Dear Committee

Treasury Laws Amendment (2022 Measures No. 4) Bill 2022

Chartered Accountants Australia and New Zealand (CA ANZ), CPA Australia and the Institute of Public Accountants (IPA) ("**the Joint Accounting Bodies**") welcome the opportunity to provide a submission to the Economics Legislation Committee ("**the Committee**") on the *Treasury Laws Amendment (2022 Measures No. 4) Bill 2022* ("**the Bill**") that was referred by the Senate on 24 November 2022. Together, the Joint Accounting Bodies represent over 350,000 professional accountants in Australia, New Zealand and around the world. Our members work in diverse roles across public practice, commerce, industry, government, and academia.

In this submission, we have focused our feedback on:

- **Schedule 6** to the Bill which amends the *Corporations Act 2001*, the *Australian Securities and Investments Commission Act 2001* (the "ASIC Act") and the *Superannuation Industry (Supervision) Act 1993* (the "SISA") to extend and adapt the financial reporting and audit requirements in Chapter 2M of the Corporations Act to apply to Registrable Superannuation Entities ("**RSEs**") for reporting periods commencing on or after 1 July 2023.
- **Schedule 9** to the Bill which amends various taxation laws to confirm the tax treatment of certain defined benefit pensions following the Full Federal Court decision in *Commissioner of Taxation v Douglas [2020] FCAFC 220* (the "Douglas decision"). This Schedule also provides a non-refundable tax offset for recipients of invalidity benefits paid in accordance with the Military Superannuation and Benefits Scheme (MSBS) or the Defence Force Retirement and Death Benefits Scheme (DFRDBS) to ensure they do not pay additional income tax because of the Douglas decision.

Schedule 6 – Financial reporting and auditing requirements for superannuation entities

We acknowledge and thank the Government for acting on the feedback in our previous submission in its decision not to proceed with the introduction of interim financial reporting and sub-fund financial reporting for RSEs.

While we agree that there is a need to clarify the requirements around, and increase the transparency of, reporting by RSEs, we note that the Explanatory Memorandum states this measure has a "low" compliance cost impact. We are unable to locate a cost-benefit analysis, or any other evidence to support such a claim. Whilst it is the case that RSEs must prepare their financial reports using relevant Australian Accounting Standards – especially AASB 1056 *Superannuation Entities* – introducing statutory financial reporting and audit requirements for RSEs will have a compliance cost impact that is greater than "low".

RSEs will face implementation costs in the first three to five years, which may be substantial depending on entity circumstances, including reviewing the additional requirements and assessing these in the RSE's context and establishing processes to meet and monitor these requirements.

RSEs may incur potentially substantial additional ongoing compliance costs, including performing any additional processes and external reporting or assurance required, as well as dealing with a new regime/regulator and managing how this interacts with obligations under existing legislation and regulations as outlined below. In the current constrained market for reporting and audit expertise, the costs of recruiting additional resources to deal with the changes will be exacerbated. Moreover, the substantial penalties, many of which involve strict liability and hence may apply even in the absence of fault or criminal intent, are likely to encourage trustees to invest more heavily in compliance and resourcing over and above minimum requirements.

It is also the case that the Australian Securities and Investments Commission (ASIC) will incur greater costs to collect and assess the financial reports from RSEs. These costs will be passed on to RSEs through the ASIC Industry Funding Model.

The total additional costs incurred by RSEs will vary from entity to entity. Nevertheless, we believe that these additional costs cannot be described as "low". Ultimately, it will be fund members who will bear these additional compliance costs incurred by RSEs, which comes at a time when RSEs are being strongly encouraged to focus on cutting costs to improve member outcomes.

The imposition of strict liability for breaches of the auditing and assurance standards issued by the Auditing and Assurance Standards Board ("the AUASB standards") (section 307A of the Corporations Act) continues to be a major concern for the auditing profession. If charged with a strict liability offence, the prosecution does not have to prove intention, knowledge, recklessness or even negligence. This leads to liability regardless of fault and potentially imposes criminal liability, which is arguably not appropriate when principles-based standards are being used (i.e., the AUASB standards) and which require a subjective determination of compliance. In applying the AUASB standards, auditors use their professional skill and scepticism to exercise judgement. Strict liability in this context is unique to Australia. By contrast, in similar regimes overseas, such as the United Kingdom, United States, Hong Kong and Singapore, liability depends on either the intentional or negligent infliction of harm. We recommend that the auditor liability settings under this proposed regime are aligned with the rest of the world.

We encourage a whole of government approach to regulatory policy. Therefore, this package of measures should be viewed holistically with other similar transparency projects either underway or recently completed for RSEs, such as:

- Portfolio holdings disclosure, which commenced on 31 December 2021.
- The member outcomes requirements, administered by the Australian Prudential Regulation Authority (APRA), which commenced on 1 January 2020.
- The design and distribution obligations, administered by ASIC, which commenced on 5 October 2021.
- The performance testing regime, administered by APRA, which commenced on 1 July 2021.
- Reporting requirements set by section 29QC of the SISA, designed to ensure that information provided to APRA as part of fund reporting can be equated with similar information required by ASIC. These are yet to come into effect.

Additionally, we note the commitment made by the Assistant Treasurer and Minister for Financial Services, the Hon. Stephen Jones MP in the media release on 23 November 2022, to overhaul transparency requirements for funds. The announcement proposes to align reporting requirements of funds with publicly listed companies, launch a new granular transparency report and reform existing reporting to reduce duplication and enhance clarity.

Schedule 9 – Taxation of military superannuation benefits: Reversing the Douglas decision

The Joint Accounting Bodies support Schedule 9 to the Bill, as it resolves the uncertainty created by the Douglas decision in relation to existing defined benefit pensions paid due to invalidity. However, there is an important policy question posed by both the Douglas decision, as well as the Bill.

Schedule 9 of the Bill follows the decision of the Full Federal Court in the Douglas decision, which considered on appeal the status of invalidity payments made under the Military Superannuation and Benefits Scheme (MSBS) or the Defence Force Retirement and Death Benefits Scheme (DFRDBS). In short, the case found that benefits paid under pensions provided on or after 20 September 2007 are superannuation lump sum benefits and, where provided prior to that date, are superannuation income stream benefits.

The Bill is intended to ensure that the Douglas decision only affects payments made from those schemes referred to in the previous paragraph. It does this by introducing a definition into the *Income Tax Assessment (1997 Act) Regulations 2021* (ITR97-2021) at Regulation 307-70.02 to ensure that defined benefit pensions which fall within regulation 1.03 of the *Superannuation Industry (Supervision) Regulations 1993* (SIS Regs) paid from a defined benefit superannuation fund or an exempt public sector superannuation scheme (but are not invalidity pay or pensions paid from the MSBS or DFRDBS) are classed as complying superannuation income streams, where these are commenced on or after 20 September 2007.

In addition, the Bill introduces a non-refundable tax offset to ensure that members of the DFRDBS or MSBS are not adversely affected by the impact of the Douglas decision, as well as recipients of spouse or children's pensions paid under the schemes.

We note that successive Government reviews, including the recent Retirement Income Review, have repeatedly underlined the importance of superannuation benefits paid as income streams rather than lump sums. We raise concerns that, even though the separate investment incentives obtained via taxation as well as otherwise (e.g., time in the market, concessional social security treatment etc.) are designed to favour superannuation benefits taken as income streams, there still appears to be an opportunity to arbitrage between the tax treatment for benefits paid as lump sums and the tax treatment for income streams. Leaving aside the tax and other separate concessions designed to encourage investment, benefits paid to members of superannuation funds should avoid such opportunities for arbitrage. We note that in both the DFRDBS and MSBS most invalidity benefits paid to members of those schemes are paid as pension payments.

While we do not necessarily support the principle of tax parity at the point of the taking of benefits, we do support measures designed to encourage the taking of superannuation benefits as income streams compared to lump sums. We note that parity already exists for members aged over 60 in fully funded arrangements and are aware that existing the tax treatment for those aged under 60 is designed to reflect several historical practices created through taxation methods in the accumulation phase. However, the decision to ensure that parity is in place for recipients of invalidity benefits from MSBS or DFRDBS, via the use of non-refundable tax offsets, is likely to be of acute interest to members of other schemes where the option to take benefits as lump sums versus income streams arises.

Consequently, we consider that this is a missed opportunity to review the policy intent behind the taxation of payments from superannuation schemes.

Additionally, it is our view that the superannuation benefit payment provisions in the *Income Tax Assessment Act 1997* (ITAA97), ITR97-2021 and various parts of the SIS Regs – in particular Parts 1A (annuities and pensions) and Part 6 (payment standards) – do not align well and are in need of a significantly detailed review to remove inconsistencies. The Douglas case came about because of these inconsistencies. Whilst the proposed non-refundable tax offset solves the problems identified in the Douglas decision, we believe it would be better to remove all inconsistencies at their source rather than use a "band-aid" solution.

Finally, we note that the intention is to change both the ITAA97 and the ITR97-2021 via an Act of Parliament. We understand the rationale for this proposal, including the possibility that these proposed amendments to ITR97-2021 may not be subject to a disallowance motion, despite the assertion in paragraph 9.54 of the Explanatory Memorandum. However, it is our preference that the ITR97-2021 changes be made in their typical manner – that is, via the Governor-General in Council – as this will make it easier to identify successive regulatory changes in future.

Should you have any questions about the matters raised in this submission or wish to discuss them further, please contact Richard Webb, Policy Advisor Financial Planning and Superannuation at CPA Australia at [redacted] and Tony Negline, Superannuation Leader at CA ANZ at [redacted]

Yours sincerely

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