Federal Budget 2021–22

FSC submission

February 2021

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1 About the Financial Services Council

The FSC is a leading peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks and licensed trustee companies. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing $3 trillion on behalf of more than 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange, and is the fourth largest pool of managed funds in the world.

2 Executive Summary

The FSC welcomes the opportunity to contribute to the Pre-Budget submission process for the 2021–22 Budget. As Australia's economy recovers from the impact of COVID-19, the Government should prioritise action on a number existing policy commitments to support this process this submission details.

Prioritisation of these issues will improve productivity and consumer outcomes, improve certainty, increase competition and cut red tape.

In addition, the Budget should benefit in the longer term from reform because the changes advocated by the FSC will increase income and tax revenue, improve retirement incomes while reducing the costs of the Age Pension.

In some cases, the Government should refrain from acting – so this again will not require substantial action.

3 Recommendations

The FSC recommends the Government:

a) Introduce a **comprehensive product modernisation (or product rationalisation) scheme** for legacy products in financial services. The Government has a long-standing commitment, made in 2015 in the Government's response to the Financial Systems Inquiry (**FSI**),[1] to implement such a scheme for life insurance and funds management, and the FSC advocates this commitment be extended to superannuation. This is discussed further in Section 4.
b) prioritise implementing existing commitments, as outlined in Attachment A, to:

[1] See inquiry recommendation 43 – legacy products, and the Government's response outlined here - https://www.treasury.gov.au/publication/government-response-to-the-financial-system-inquiry/attachment-government-response-to-financial-system-inquiry-recommendations

- address **outstanding Investment Manager Regime (IMR) issues** – a commitment the Government made in 2017;
- **extend the attribution regime** to Investor Directed Portfolio Services – a Government commitment from 2017;
- Legislate for the **permanent Capital Gains Tax (CGT) rollover relief for merging superannuation funds** – a Government commitment from 2019;
- **Expand the functional currency election to certain trusts and partnerships** – a Government commitment from 2013; and
- **fix outstanding issues with the Taxation of Financial Arrangements** – a commitment from 2017.
  - An alternative and simpler approach to improve the competitiveness of managed funds is to implement a 5% rate of Non-resident Withholding Tax (NRWT) on Asia-Region Funds Passport payments, excluding income from Australian real property. The detailed argument for this change is in Attachment B.
- **Widen the eligibility for the functional currency election** to certain trusts and partnerships.

c) Building on the Government's announcement to "modernise and expand" Australia's tax treaty network, **prioritise tax treaties with Luxembourg and Hong Kong**, addressing financial services issues in existing tax treaties, and ensuring that any new Free Trade Agreements are accompanied by a tax treaty.
   - The FSC welcomed the announcement in the 2020-21 Budget for this review of the tax treaty network, and considers treaties with Luxembourg and Hong Kong should be a priority, as explained in detail in previous Budget submissions.[2]
   - This would be consistent with the Government response to industry's Action Plan to boost Australian services exports, where the Government committed to "assessing Australia's [tax] treaty network to ensure it remains appropriately aligned to our trading relationships, whilst maintaining tax system integrity" (page 25).[3]
   - In the 2020-21 Budget, the Government also indicated it will "prioritise refurbishing Australia's treaties with key strategic partners where necessary to maximise the benefits for Australia's economy" – the FSC considers that older tax treaties should be amended so they fully deal with superannuation funds and collective investment vehicles.[4]

d) Building on the announcement of a reformed corporate residency test (announced in the 2020–21 Budget), make a commitment that the changed test will apply to corporate limited partnerships as well.

e) not proceed with two previously announced proposals – see details in Attachment C:

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[2] See FSC Pre-Budget submission for 2019–20 and 2020–21, available from FSC website: https://fsc.org.au/resources?search=budget

[3] See: https://dfat.gov.au/about-us/publications/Pages/action-plan-to-boost-australian-services-exports.aspx

[4] See FSC Pre-Budget submission for 2019–20 and 2020–21.

- **The proposal to remove the CGT discount at fund level for Managed Investment Trusts (MITs) and Attribution MITs (AMITs) should not proceed**, and instead be replaced with a measure targeted at the small proportion of investors that are inappropriately accessing the CGT discount through MITs and AMITs.
- the Government should **not proceed with proposed changes to AMIT penalties**.

f) Address a number of technical tax issues, covered in a previous submission of the FSC, at Attachment D, including the following:
   - Allow AMITs to access CGT rollover relief that is available to other trusts.
   - Treat gains or losses on bond sales as interest, given these gains are equivalent to interest in economic substance.
   - Ensure the correct Australian taxation of foreign capital gains.
   - Provide flowthrough tax treatment for foreign trusts.

g) if unfavourable changes occur to the Offshore Banking Unit (**OBU**) regime, place additional priority on the FSC's requested changes outlined above in items (a) to (e).

h) **lower the tax on new investment**. The FSC's preferred approach is a reduction in the company tax rate to 25%, or ideally a lower rate. However, if this reform is not achievable, then the Government should implement one or more alternatives which could include:
   - Providing accelerated depreciation or an investment allowance, as recommended by the Business Council of Australia.[5] Such an approach should not discriminate between types of investment but should be broadly applied.
     - We note an investment allowance is simple to implement for corporate entities. However, for tax flow-through trust structures such as MITs and AMITs, the benefits of the allowance may be 'washed out' through cost base reductions for unitholders upon distributions.
     - Therefore, there should not be a cost base reduction in order for investors through MITs and AMITs to benefit from the allowance.
     - If this does not occur, then direct investment would be preferentially taxed relative to indirect investment, which would operate contrary fundamental tax principles for indirect investment vehicles.
   - A targeted reduction in tax for companies that expand employment.
   - Reducing the taxation on new equity investment such as through an Allowance for Corporate Equity.

i) **Address complexities with the superannuation transfer balance cap** – see Section 5 below.

j) The Intergenerational Report (IGR), due to be released in the middle of this year, should include **estimates of the long-term impact of the superannuation system** on the Budget, particularly the Age Pension. This includes the impact on numbers of full and part pensioners and the dollar spending on the Age Pension, and the extent to which superannuation savings will fund other age-related expenses, such as

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[5] See: https://www.bca.com.au/strong_budget_strong_economy_strong_australia

health and aged-care costs, reducing individuals' overall reliance on the Government in retirement.

k) Ensure Australians can access affordable financial advice through incentives such as tax deductibility at a capped amount enabling reduced reliance the Age Pension long-term while improving National Savings.

l) Extend supports for financial services that help strengthen the Digital Economy by reducing cost, improving compliance and incentivising data and technology-driven efficiencies across the financial services industry.

m) Target measures to assist the restoration of superannuation balances that include a co-contribution scheme, a concessional cap for those aged over 50 years of age, and a steady increase in the preservation age to 62.

n) The Government provide **clarity about the development of the Corporate Collective Investment Vehicle** (**CCIV**). This important reform has been significantly delayed and its future is unclear. In addition, the most recent draft of the CCIV rules failed to meet commitments that the CCIV would have equivalent tax treatment to AMITs, and also included the unfavourable tax changes outlined in point e) above.
    - Australia is currently at a disadvantage compared to other countries that have a corporate vehicle for managed funds, particularly in our ability to utilise the Asia-Region Funds Passport. The long-anticipated CCIV would ideally address this problem.

4 Product modernisation

While Australia's economy recovers, consumers still have significant amounts of money trapped in out of date financial products that can result in poor customer outcomes, including high fees and poor returns. Australians are being substantially disadvantaged by being locked into these legacy products that lack the better returns, better features and easier access of more modern products. Financial services businesses are unable to move customers into more modern products for reasons including large tax or social security penalties (the numerous reasons for product lock-in are detailed in Section 4.3 below).

Acknowledging this problem, the Government some time ago (2015) announced it would implement a comprehensive product modernisation (or product rationalisation) scheme for legacy products in financial services. The FSC is urging the Government to implement this already existing commitment, which is clearly overdue.

4.1 Legacy products are an extensive (and expensive) problem

The Productivity Commission in its 2019 report into the superannuation industry[6] highlighted the extent of the problems caused by legacy products in superannuation alone. The Productivity Commission found in 2017:[7]

- there was $162 billion invested in legacy superannuation products, which is 10% of the total assets held in APRA-regulated funds.
- there were 3.2 million legacy member accounts, which is 12% of the total for APRA-regulated funds.
    - This implies around 2 million individuals were trapped in legacy superannuation products with poor returns, based on the number of duplicate accounts in 2017.[8]
- Legacy products made up 46% of the assets in the high fee tail of products, with about 2 million member accounts; and almost all legacy products have high fees. The average fee in this tail was 2.2%, which is more than three times the most prevalent (i.e. modal) fee of 0.7% (see page 180 of the report).
- The number of products in the high fee tail has remained steady over time (see page 180 of the report). This implies that it cannot just be assumed that the issue of legacy products will gradually disappear over time (see further discussion in Section 4.4 below).

The figures above do not include legacy products outside of superannuation such as life insurance and managed funds, which are likely to be substantial. Earlier estimates of the extent

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[6] Productivity Commission (2018) *Superannuation: Assessing Efficiency and Competitiveness*, Report no. 91

[7] Productivity Commission (2018), Page 115 except where stated.

[8] There were about 1.6 accounts per person in 2017, see: https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Super-statistics/Super-accounts-data/Multiple-super-accounts-data/

of the issues are contained in previous FSC submissions[9] and the FSC is planning to conduct a survey of our members to update these figures in the near future.

4.2 Adverse impact of legacy products

There are numerous adverse effects from legacy products. In general, legacy products when compared to modern products can have:

- lower net returns, in many cases resulting in lower retirement incomes.
- higher fees – often significantly higher. The Productivity Commission evidence referred to in Section 4.1 above shows legacy products in superannuation have fees that are more than three times the most prevalent fee rate.
- poorer consumer disclosure and reporting.
- increased likelihood of errors, as many processes have to be completed manually.
- worse regulation for consumer targeting and suitability, as legacy products were sold before the introduction of the Design and Distribution Obligations (DDO) regime.
- worse technology and reduced accessibility, for example they are not accessible through the internet or via apps.
- reduced resilience, as systems are out of date and expensive to maintain.

At an economy wide level, the trapping of consumers in these products:

- reduces financial services innovation:
    - innovation can create legacy products, because a pioneering financial product may have low take up, and as a result be closed to new members. These products will then over time become legacy products – and the lack of a modernisation scheme will mean customers are trapped in the products and the products eventually become out of date and costly to operate. Businesses can avoid this risk if they avoid innovation.
    - this is especially a problem for long-dated products such as innovative retirement income products which can easily become legacy products if take up is low (see also the discussion in Section 4.4 below).
- adds to product proliferation – this undesirable proliferation is not by consumer choice.
- increases financial system risks.
- reduces competition in financial services, as consumers trapped in legacy products cannot move to competing products.
- reduces scale economies, increasing industry costs.
- reduces the productivity of financial services, dragging down economy-wide productivity.
- reduces savings and wealth.

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[9] For example see FSC Pre-Budget submission for 2018–19, available from: https://consult.treasury.gov.au/budget-policy-division/2018-19-pre-budget-submissions/consultation/download_public_attachment?sqId=question.2017-09-12.3768452384-publishablefilesubquestion&uuId=596571344

- increases Government spending on income support, particularly the Age Pension, because of reduced retirement savings.
- reduces tax revenue because lower income/investment returns reduce income tax revenue.

The final two points imply that the lack of a modernisation scheme is likely to have an adverse impact on the Government Budget. While it may appear that a product modernisation scheme would cost the Government money in the short term, in the longer term a modernisation scheme may be a net benefit to the Budget as it will boost tax revenue and reduce Age Pension spending.

We also note that legacy products are more likely to pay commissions until the legislative ending of commissions. A product modernisation scheme would move consumers into products that are highly unlikely to pay commissions. The ending of commissions through product modernisation will reduce fees and improve net returns.[10] In addition, this would avoid the issues that may occur with the legislative ending of grandfathered commissions, including the complexity of redirecting commissions to consumers and the possibility of a legal challenge to the legislation as reported in the media.

4.3 Barriers to product modernisation

It might be thought that financial services businesses could just transfer customers out of inferior legacy products. However, there are various taxes, rules and regulations that prevent this occurring, including:

- Legal requirements that stop providers from changing consumer rights without explicit consumer consent. Broadly, superannuation deals with this issue in some circumstances - but this issue is not addressed outside of super.[11]
    - For example, the provisions in individual fund constitutions or policies for a non-super investment product may not allow for transferring customers to another trust or policy.
        - In that case, consent would be required from all customers which would include uncontactable customers.
    - It would be problematic to transfer just the customers who are contactable and agree to the transfer: moving only some customers to modern products might make those customers better off but might make the remaining customers worse off, because high costs are spread over fewer remaining individuals.
- The imposition of Capital Gains Tax (**CGT**) on unrealised gains. This tax can be imposed on the consumers holding the relevant legacy investment product, and also on the vehicle making the investments.

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[10] This is discussed in more detail in the FSC's submission on the Draft Regulations for Ending Grandfathered Conflicted Remuneration for Financial Advisers, available from: https://fsc.org.au/resources/1756-fsc-submission-ending-grandfathered-conflicted-remuneration-for-financial-advisers-13th-may-2019/file

[11] See FSC submission to 2019–20 Budget.

    - The Government has announced the permanent provision of CGT relief for merging superannuation funds.
        - This CGT relief only exists for transfers that are executed as a ‘single arrangement’ that occurs within a single tax year. This means relief is not available where there are too many members to transfer in one tranche for operational reasons.
    - The CGT issue remains unaddressed for the modernisation of products within a super fund, for life-backed superannuation products, for life insurance products, and for non-superannuation investments.
    - There is also generally an inability to transfer capital losses to new products.
- State stamp duty on investments that back a product (whether super or non-super). Stamp duty typically applies to land held through unit trusts and companies.
    - The CGT rollover relief for merging super funds noted above does not deal with this stamp duty problem.
- For life insurance bonds, potential for re-starting of the 10 year rule.[12]
- Legal barriers that restrict the ability for product providers to communicate with members of legacy products about contemporary products.
- Possible loss of legislated member elections/decisions, for example binding death benefit nominations and elections as a result of the Protecting Your Super **(PYS)** and Putting Members Interests First **(PMIF)** legislation.
- In some cases, any customer transition to a modern product must be done with client consent, generally based on financial advice. Given the cost of personal advice, this may act as a significant barrier to rationalisation.
- Loss of grandfathered social security treatment. For example (highlighting added):

> *a person who is an owner of an account-based pension purchased before 1 January 2015 and the holder of a CSHC [Commonwealth seniors health card] on 31 December 2014, will not have their account-based pension included in the income test for as long as they: continue to hold a CSHC,* ***and retain the same account-based pension.***[13]

To emphasise the points above, product modernisation relating to superannuation still faces numerous barriers even though some components have been addressed.

We welcome the Government’s announcement of changes to commutation rules for certain legacy income stream products, including the removal of ‘unfair tax liabilities’, announced in the 2020–21 MYEFO. This will partly address the issue of legacy products in superannuation, and the FSC looks forward to discussing the details of this measure with the Government. However, the need for a comprehensive rationalisation scheme for superannuation still remains, including the option for the complete rationalisation (rather than partial commutation) of legacy income stream products.

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[12] See: https://www.moneysmart.gov.au/investing/complex-investments/investment-and-insurance-bonds
[13] See: https://guides.dss.gov.au/guide-social-security-law/3/9/3/31

4.4 The problems of legacy products are unlikely to disappear

There is a perception that legacy products are a 'one off' problem that will gradually solve itself over time, for example as customers of legacy products close or withdraw remaining balances in the products. As a result, it might be thought that inaction on this issue is less of a concern. However, this view does not fit with the data outlined in Section 4.1 above showing the number of legacy products has not declined over time.

The Productivity Commission has also stated there is "strong risk that the incidence of legacy retirement products will rise".[14] They reached this conclusion because:

- product innovation and policy developments suggest annuities and pooled investments will grow in prominence;
- products will reflect tax and social security policy settings at the time of issuance; and
- as these settings change, or if innovative products fail to gain sufficient interest, some products may become obsolete.

4.5 History of product modernisation proposals

There has been a long-standing recognition of the need for a product modernisation scheme to allow consumers to move from legacy products to newer products. The FSC first put forward a proposal for a product modernisation scheme to the Government in July 2005 and in other forums since then.[15]

As early as 2006, the Productivity Commission recommended product rationalisation in its report 'Rethinking Regulation' stating:

> *"The Taskforce considers that implementing a simplified product rationalisation mechanism that could be applied to the full spectrum of financial products would significantly improve operational efficiency and reduce the operational risks carried by financial entities."*[16]

The Superannuation System Review (**the Cooper Review**) argued in June 2010:[17]

> *The consolidation and rationalisation of legacy products can provide benefits to members, including:*
>
> - *better product disclosure and clearer reporting to members;*
> - *lower costs — as cost savings will be passed on to members;*

[14] See Productivity Commission (2018), page 216.
[15] For example: Phase Two submission to FSI; and Product Rationalisation — Managed Investment Schemes and Life Insurance Products Proposals Paper, 26 February 2010.
[16] Rethinking Regulation: Report on the Taskforce on Reducing the Regulatory Burden on Business (January 2006) See: https://www.pc.gov.au/research/supporting/regulation-taskforce/report/regulation-taskforce2.pdf
[17] https://treasury.gov.au/review/super-system-review

- *enhanced and newer features, for example, BPay, internet/online transactions, investment choice, unbundled offerings, more transparent and easier to understand products; and*
- *improved service standards through better administration, greater flexibility, fewer systems and processes.*

> *Such benefits result principally from greater economies of scale and transfers to more modern and flexible products and systems.*

ASIC made the following submission to the interim report of the Financial System Inquiry (**FSI**) in August 2014:[18]

> ASIC supports renewed consideration of the 2009 proposals on product rationalisation of legacy products by Government.
>
> …
>
> We support an approach developed from the 2009 proposals that provides a streamlined process for product rationalisation involving adequate disclosure and safeguards, without requirements of individual holder assent.

A product modernisation scheme was an important recommendation of the FSI final report in 2014:[19]

> **Recommendation 43: Legacy products**
>
> Introduce a mechanism to facilitate the rationalisation of legacy products in the life insurance and managed investments sectors.

In response to the final report, the Government made the following commitment in 2015:[20]

> The Government agrees to facilitate the rationalisation of legacy products, in light of consumer, constitutional and fiscal issues.
>
> It is important that consumers should not be worse off due to any transition to a newer product. Under the existing framework there are possible tax implications of facilitating the transition away from legacy products, which will be explored in the context of the Government's Taxation White Paper process.

ASIC report 466 *ASIC's work to reduce red tape* stated in January 2016:[21]

> ***Legacy product rationalisation***

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[18] https://download.asic.gov.au/media/2613736/asic-submission-to-the-financial-system-inquiry-interim-report-published-26-august-2014.pdf
[19] http://fsi.gov.au/publications/final-report/executive-summary/#recommendations
[20] https://static.treasury.gov.au/uploads/sites/1/2017/06/Government_response_to_FSI_2015.pdf
[21] https://asic.gov.au/regulatory-resources/find-a-document/reports/rep-466-asic-s-work-to-reduce-red-tape/

> *Submissions suggested that a process be developed to rationalise legacy products. We agree that this would enable more efficient and up-to-date financial products and services to be provided to consumers, and avoid ongoing operational risk and cost associated with maintaining legacy products and systems. We have suggested implementing a process for legacy product rationalisation that balances the interests of consumers and product and service providers.*

An APRA submission to an Inquiry by the Senate Economics Committee into the *Scrutiny of Financial Advice – Life Insurance* of April 2016 stated:[22]

> *One area of potential change identified by APRA relevant to this Inquiry is the introduction of a mechanism to allow the rationalisation of legacy products to occur more easily…*
>
> *Over time, legacy products become more complex and expensive to administer and may no longer meet the requirements of the beneficiaries…*
>
> *There is a range of very complex legal, consumer and tax issues that arise if a life insurer seeks to move policyholders from a legacy product to a new product, restricting the ability of insurers to close legacy products. The benefits of a simpler, though still robust, mechanism to rationalise legacy financial products has been recognised for some time…*
>
> *APRA continues to strongly support the need to comprehensively address this issue. From the perspective of the product provider, it would help mitigate the increasing operational risk that such products create, as well as improve the industry's operational efficiency. From the consumer perspective, it has the potential to improving consumer outcomes by updating definitions, improving efficiency and administration, and lowering costs.*

The final report of an Inquiry by the Parliamentary Joint Committee on Corporations and Financial Services into the Life Insurance Industry stated the following in March 2018:[23]

> ***Recommendation 10.13***
>
> *The committee recommends that the Australian Government introduce legislation to facilitate the rationalisation of legacy products*

The Productivity Commission inquiry into superannuation said the following in 2018:

> *[APRA should] undertake a systematic assessment of the costs to funds of the thousands of legacy products in the superannuation system. If the evidence demonstrates that they represent a significant cost in accumulation, APRA should*

[22] https://www.apra.gov.au/sites/default/files/APRA-submission-to-Financial-Advice-Life-Insurance-Inquiry_1.pdf

[23] https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/LifeInsurance/Report/b02

> *further refine trustees' obligations for member transfers so these products can be rationalised.*[24]

The Treasury stated the following in a background paper on the life insurance industry, written for the Royal Commission into Financial Services in August 2018:[25]

> *The products that the life insurance industry offers are continually revised and updated. Products are often deemed uneconomic or dated as a result of changes in market structure, government policy or legislation. These legacy products increase costs to insurers, which may be passed on to consumers. They may also increase operational risks in the management of products, which can lead to administrative errors that affect consumers. In rationalising these outdated products consumers and the industry can benefit from new, more efficient products.*
>
> *There are challenges to achieving this rationalisation of legacy products fairly and effectively. For example, a capital gains taxation (CGT) taxing point may arise if life company assets are transferred to another life company or a custodial arrangement as part of the rationalisation.*

Despite these observations, no noticeable progress has been made on a regime for product modernisation.

4.6 FSC's recommended product modernisation solution

The FSC's recommended approach for the modernisation of legacy financial products is:

- a consumer interest test applied at a collective level;
- transfer of non-tax attributes (e.g. social security benefits such as account-based pension 1 Jan 2015 grandfathering);
- roll over of all tax attributes to the new vehicle; and
- no tax implications of the rollover itself (including to the extent possible the removal of any stamp duties on the rollover).

The consumer interest test involves an independent determination that modernisation is in the interests of consumers collectively.

Recommendation
Introduce a comprehensive product modernisation (or product rationalisation) scheme for legacy products in financial services. The Government has a long-standing commitment (made in 2015 in the Government's response to the FSI) to implement such a scheme for life insurance and funds management, and the FSC advocates for extending this commitment to superannuation.

[25] https://financialservices.royalcommission.gov.au/publications/Documents/reforms-to-general-and-life-insurance-background-paper-27.PDF

Recommendation
To expedite the rationalisation of a large number of legacy products, the Government should explore the appropriateness of an institutional mechanism (e.g. tribunal) that would allow for expert independent decision-makers to approve rationalisation of products. This would help address the concerns of both consumers and industry by providing greater certainty, transparency and timeliness around a process that has historically proved difficult to negotiate.

The FSC's proposed product modernisation approach, as provided to the Financial Systems Inquiry in 2014, is in Attachment E.

5 Transfer balance cap

5.1 Issue

The superannuation system now has several caps on contributions and a cap on the maximum amount that can be transferred into retirement phase accounts (the Transfer Balance Cap or **TBC**). These caps add substantial complexities to the superannuation system. The upcoming indexation of the TBC is a case in point.

The general TBC is indexed by increments of $100k, but the actual value of the cap will be a different amount below $100k for all individuals who have some money in retirement phase already. Specifically:

- A superannuation fund member who only has $160k in retirement phase has only used up 10% of the $1.6m of the general TBC. So they have 90% leftover of the general TBC. Under the legislation, they have 90% or $90k added to their own personal TBC (taking it up to $1.69m) at that point in time.
- A member who has $1.44m in retirement phase has used up 90% of the $1.6m general TBC. So they have 10% leftover of the general TBC. Under the legislation, then they only get 10% or $10k added to their own personal TBC (taking it up to $1.61m) as at that point in time.

As a result, every person who has entered into retirement phase will have a different and personal TBC.

This issue will be faced in the near future when the general TBC is indexed from 1 July 2021,[26] meaning the personalised TBC issue will be faced from that day onwards.

5.2 Comment

When the Budget measures were introduced, the Government and industry were focussed on delivering the initial transfer balance account values and turning off the monitoring of various contribution caps and transition to retirement income streams (**TRIS**). There was not a need for the Government or industry to focus on the issue of indexation, but this issue is now of more relevance.

The superannuation industry has not in its recent history experienced any caps that vary between individuals in such a way.

In the near future, the ATO will calculate every taxpayer's personal TBC. However:

- The calculation of the TBC is complicated and complexity will increase over time with each indexation of unused caps;
- The situation is difficult to explain to members; and

[26] https://www.ato.gov.au/Individuals/Super/In-detail/Withdrawing-and-using-your-super/Indexation-of-Transfer-balance-cap/

- The individualised TBC is hard for trustees or financial planners to advise on if they are unaware of a customer's total super balances (e.g. if the customer has accounts with several providers).

There is a particular issue of concern to FSC members if fund members act on a personal TBC calculation if this is based on incorrect data. In some cases, the fund member could be subject to a penalty for an error outside their control. The issue is exacerbated if a customer has interests in an SMSF (in addition to an APRA regulated fund) which do not need to report as quickly as APRA regulated funds. Some degree of leniency in administration is warranted.

The FSC recommends the Government consider methods for reducing this complexity, for example:

- There could be one indexed TBC for everyone, regardless of when individuals transferred into a retirement phase account, or how much is in the retirement phase.
- As an alternative, the proportionate reduction for unused caps could only apply at the higher end (i.e. those close to the TBC in the previous year), as opposed to the entire retiree population.
- The TBC could be replaced by taxation of income from retirement phase accounts above a high tax free threshold that mirrors the effect of the TBC.

A large majority of retirees will never get close to $1.6m for the proportional reduction calculation to matter, so the current approach is costly and inefficient to administer and calculate for the majority.

6 Restoring Superannuation Balances

While superannuation plays a significant role in Australia's economic recovery, the COVID-19 pandemic has impacted savings across the sector, with the industry-wide rate of return for the March quarter being -10.3 per cent.[27]

Markets have recovered in the intervening months, however ongoing volatility would likely have impacted retirement planning, especially for those in the later years of their working lives. The market recovery has also varied greatly across different asset classes.

Recommendation
The FSC recommends targeted measures to help these categories of Australians rebuild their retirement savings, including:

- A co-contribution scheme for members who participated in the hardship policy, where the Government contributes $1 for every $5 in voluntary contributions made by a member (to a maximum $10,000 member contribution);
- A concessional cap of $50,000 for those over the age of 50 years for the 2020-21 financial year, with the option of 'carrying forward' unused value; and
- A steady increase in the preservation age to 62 years, to promote mature-age workforce participation and restore the 5-year link to the Age Pension eligibility.

[27] APRA (2020) Quarterly superannuation performance statistics highlights, March 2020.

7 JobMaker Digital Business Plan

Financial services and the Digital Economy are interlinked. The FSC welcomes the Federal Government's commitments to this area outlined in Federal Budget 2020 through its JobMaker Digital Business Plan. In particular, the FSC welcomes the following commitments:

- Investment in a regulatory commercialisation initiative to improve compliance
- Consultation on making permanent temporary reforms to allow companies to hold virtual meetings and execute documents electronically
- Improvements to the Modernising Business Registers program
- Support for small business to take advantage of digital technologies
- The compliance and regulatory burden for financial services is considerable. This can have the unintended consequence of limiting the innovation and capability of financial services firms and, by example, in the financial advice sector, see much of this cost passed to consumers.

Investment in data-driven technology to increase efficiency, simplify compliance and lower costs for businesses and consumers.

Recommendation The FSC would welcome similar measures in the forthcoming Federal Budget to support the digital economy and the role of financial services in strengthening it.

8 Ensuring Australians can access affordable financial advice

COVID-19 has seen a surge in demand for professional financial advice on a range of matters such as redundancy, pensions, retirement and estate planning, life insurance, and early access to super with many advisers servicing this need. Cost, and the compliance burden behind that cost, are the biggest barriers to delivering and receiving financial advice to support good financial decision-making by consumers.

Recommendation
The Government should explore the tax deductibility of all financial advice at a capped amount to incentivise good financial decision-making by consumers and accommodate the Government's concerns for any fiscal implications.

Some types of financial advice are already tax deductible, such as that which can be attributed to the management of a particular (taxable) asset or investment or types of life insurance. Some types of payments to financial advisers were previously effectively tax deductible,[28] and this formed part of the remuneration of advisers. Changes in the payment structures for advisers has closed an avenue for effectively tax deductible advice, and tax revenue for the Government has likely increased due to this change.

Tax deductions on professional and well-regulated financial advice will support decision-making by consumers impacted by the economic upheaval with a number of positive outcomes:

- Research consistently attributes improved mental health and wellbeing outcomes to the receipt of professional financial advice[29]
- Rice Warner's *Future of Advice Report* released by the FSC in October 2020 included modelling showing the relief an advised population can have on government spending on the Age Pension as well as improved National Savings[30]
- Advice supports decision making that benefits the economy (e.g. debt management) and improves savings behaviour
- Consumers accessing professional financial advice will relieve pressure on the social services, financial counselling community and voluntary sector whom the Government would intend should cater to higher needs consumers
- Prior to the pandemic, research by Adviser Ratings in 2019 showed average funds under advice totalled $61 million and average client assets were about $650,000 suggesting advisers are working with middle Australia where there is fee pressure.[31]
- The number of financial advisers dropped below 21,000 in the last year which further limits access to professional financial advice.[32]

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[28] Commissions often came from investment returns that would be otherwise taxable. Conversely the rebates of commissions are being treated as assessable, see: https://www.ato.gov.au/Individuals/Income-and-deductions/In-detail/Compensation-payments/Payments-of-conflicted-remuneration/

[29] Rice Warner Future of Advice report: RW-Future-of-Advice-Report.pdf (ricewarner.com)

[30] Rice Warner Future of Advice report: RW-Future-of-Advice-Report.pdf (ricewarner.com)

[31] Adviser Ratings – 2019 Advice Landscape

[32] Money Management. 'Adviser numbers drop below 21,000 in November | Money Management'

9 Attachment A – Existing Government Commitments

The FSC requests the Government prioritise a number of existing commitments, in particular:

9.1 Address outstanding Investment Manager Regime (IMR) issues

From press release of 19 July 2017:

> "The Government is committed to implementing an effective IMR whilst maintaining the integrity of our residency rules. The Government will therefore consult on whether a legislative amendment is required to ensure that the engagement of an Australian independent fund manager will not cause a fund that is legitimately established and controlled offshore to be an Australian resident." See: http://kmo.ministers.treasury.gov.au/media-release/064-2017/

9.2 Extend the attribution regime to Investor Directed Portfolio Services

From a press release of 19 July 2017:

> "While this amendment [extending AMITs to single unitholder widely held entities] will not extend to including platforms, wraps or master trusts (commonly referred to as Investor Directed Portfolio Services) in the list of deemed widely-held entities, the Government will consult with industry on broadening the eligibility for these widely held entities to access the concessional tracing rules as part of the Corporate Collective Investment Vehicle public consultation process" See: http://kmo.ministers.treasury.gov.au/media-release/064-2017/

9.3 Capital Gains Tax rollover relief for merging superannuation funds

From the 2019–20 Budget:

> The Government will make permanent the current tax relief for merging superannuation funds that is due to expire on 1 July 2020. This measure is estimated to have an unquantifiable reduction in revenue over the forward estimates period.
>
> Since December 2008, tax relief has been available for superannuation funds to transfer revenue and capital losses to a new merged fund, and to defer taxation consequences on gains and losses from revenue and capital assets.
>
> The tax relief will be made permanent from 1 July 2020, ensuring superannuation fund member balances are not affected by tax when funds merge. It will remove tax as an impediment to mergers and facilitate industry consolidation, consistent with the recommendation of the Productivity Commission's final report, Superannuation: Assessing Efficiency and Competitiveness. Consolidation would help address inefficiencies by reducing costs, managing risks and increasing scale, leading to improved retirement outcomes for members.

The FSC notes this relief does not deal with all possible situations where relief is warranted – see discussion in Section 4.3 above.

9.4 Fix outstanding issues with the Taxation of Financial Arrangements

From the 2016–17 Budget:

> The Government will reform the taxation of financial arrangements (TOFA) rules to reduce the scope, decrease compliance costs and increase certainty through the redesign of the TOFA framework.
>
> …
>
> The measure contains four key components:
>
> …
>
> A new tax hedging regime which is easier to access, encompasses more types of risk management arrangements (including risk management of a portfolio of assets) and removes the direct link to financial accounting.

From a press release of 22 December 2017:

> "Simplification of the Taxation of Financial Arrangements (TOFA) rules was announced in the 2016–17 Budget…The Government will defer the commencement of changes to the TOFA regime and the changes will now commence from income years that begin after Royal Assent. Treasury will continue to engage with stakeholders in the design of the amended rules, and to identify specific aspects of TOFA reform that could be prioritised." See: http://kmo.ministers.treasury.gov.au/media-release/126-2017/

9.5 Functional currency election

The 2011–12 Budget announced:

> The Government will allow certain trusts and partnerships that keep their accounts solely or predominantly in a particular foreign currency to calculate their net income by reference to that currency.

The Coalition Government announced it would proceed with this Policy in its announcement of 14 December 2013. See page 4 of: http://ministers.treasury.gov.au/sites/ministers.treasury.gov.au/files/2019-05/MR008-2013.pdf

10 Attachment B – Withholding tax on payments under the Asia-Region Funds Passport

The FSC considers Australia's current tax system is not competitive in the Asia Region Funds Passport. In particular, the non-resident withholding tax (NRWT) system is complex compared to other Passport countries, as a result of:

- multiple rates;
- complexity and difficulty of determining appropriate rate;
- interactions with tax treaties (including how the treaties deal with trusts);
- no overarching consistent principle of application; and
- relatively simpler approaches in competitor jurisdictions, with Singapore in particular charging a zero withholding tax rate.

The complexity of the application of Australia's NRWT means the possible tax consequences for foreign investors cannot be explained in a simple and easy to understand manner. The Passport is specifically designed for retail investors so the inability to explain tax simply will put Australia at a substantial disadvantage.

Australia's NRWT complexity means comparisons with other jurisdictions are complicated; in general Australia's regime has high headline tax rates, but a variety of exemptions which often means the actual tax paid in Australia is low. As a result, we have a lose-lose situation – a tax system that significantly impedes investment due to its complexity while delivering little revenue (see section on potential budget impact below).

NRWT comparisons are not simple, but generally show Australia is uncompetitive. By contrast, comparisons of company taxes much more clearly show Australia is uncompetitive – Australia has the highest corporate tax rate in the Passport and in some cases the Australian tax disadvantage is large.

Our uncompetitive tax regime is inconsistent with Australia's aspirations of becoming a financial centre and exporting fund management services, particularly to Asia.

Other countries are reducing their NRWT and corporate tax rates over time, making our system more uncompetitive as time passes. Therefore, if Australia does not set NRWT and company tax rates at a competitive rate determined in the appropriate international context, funds will not be invested in Australian vehicles and the ATO will receive 100% of nothing, while Australia will miss out on the revenue, jobs and growth of our funds management industry. The benefits are likely to include back end operations as well as higher value added operations such as investment management.

If Australia is unable to reduce its corporate tax rate, this emphasises the need for other tax settings, particularly NRWT, to be more competitive.

Investors will be choosing Passport products from a number of competing jurisdictions and Australia's current tax system will place Australian funds behind funds from other countries. If tax disadvantages are removed for Australian funds, then Australian fund managers will be able to compete. In addition, a globally competitive NRWT would address one of the larger barriers to the success of Australia's funds management export industry.

The Passport only allows investments into very simple ('vanilla') products such as listed equities and bonds. This means that income generated by non-resident investors will comprise dividends and interest.

Analysis of these income types shows that little government revenue from NRWT (outside of property) will be received as a result of Passport funds under existing policy settings:

- Just over 90% of Australian top 100 company dividends are franked therefore dividend withholding tax collections will be small. A portion of the remaining unfranked dividend also qualifies for conduit foreign income (CFI) exemption. For example, the unfranked component of AMP's dividends has historically been CFI and therefore withholding tax free.
- Interest will be either overseas sourced or substantially subject to an exemption (under section128F); as a result, it would not be subject to NRWT.
- Capital gains from Australian assets that are not taxable Australian real property are not subject to a withholding obligation when derived by non-residents. The permitted investment class only allows for listed equities which are all treated as non-taxable Australian real property.
    - Note the FSC is not calling for a reduction in the NRWT applying to any property income that might be received by a Passport fund (even though this income would be limited in a Passport fund).
- Some tax treaties may operate to allocate the taxation of gains to the treaty partner.
- Some of the remaining NRWT is inappropriately applied to bond profits and foreign exchange hedging, as detailed in previous FSC Budget submissions.[33]

As a result of these points, a reduction in NRWT on the Passport will have limited budget impact, however it will have significant impact on the ability of Australian managers to market their funds, as it will allow confident statements to be made about the taxation impact of investing in an Australian fund.

We also understand previous costings of this proposal have used data from the ATO's Annual Investment Income Report (AIIR). However, this data is misleading as it combines property income to foreigners and non-property income to foreigners. This means the AIIR data (at least in in its current form) is unlikely to be helpful for this costing.

We expect this change will reduce compliance costs for all funds without property income, as only one rate of withholding tax will apply. A fund with property income might face higher compliance costs from complying with the property-related NRWT, but this will be offset by a reduction in compliance costs from collapsing multiple non-property rates into one rate.

[33] For example see FSC Pre-Budget submission for 2019–20, available from: https://fsc.org.au/resources/1717-2019-20-budget-fsc-submission-combined/file

11 Attachment C – Concerns with existing Government proposals

11.1 CGT at fund level

The 2018–19 Budget announced the Government would remove the CGT at the fund level for Managed Investment Trusts (MITs) and Attribution Managed Investment Trusts (AMITs).[34]

The FSC has major concerns with this proposal.

Most importantly, the policy contradicts the Government's own stated policy goals. The 2018–19 Budget states[35] this proposal is designed to ensure that MITs and AMITs operate as genuine flow through vehicles, so that income is taxed in the hands of investors as if they had invested directly. However, the 2018–19 Budget proposal has the **opposite effect** of this policy goal.

The policy disadvantages indirect investment by individuals through MITs and AMITs compared to direct investment. It removes the current neutral treatment of individuals and replaces it with a non-neutral treatment. Using the terms from the 2018–19 Budget, under the current tax system MITs and AMITs are taxed as genuine flow through vehicles for individual investors, "so that income is taxed in the hands of investors as if they had invested directly". The proposal replaces this approach with a system that **overtaxes** individuals that invest through MITs and AMITs.

This detrimental proposal would be a key contributor to the increasing adverse policy environment for fund managers noted earlier in this submission.

The specific reasons the proposal overtaxes individuals that invest in MITs and AMITs are:

- In allocating deductible expenses against assessable income components, a MIT or AMIT would be required to allocate deductions against gross capital gains instead of only the assessable discount capital gains component; and
- In recouping prior year or current year revenue losses, the MIT or AMIT would be required to recognise as assessable income the gross amount of the capital gain rather than only the discount capital gain.

A briefing from Greenwoods HSF (see Section 2 of Attachment E) provides an example where:

- an individual would pay no tax if they invested directly; but
- the same individual would pay tax on $500 if they invested in exactly the same way, but through a MIT.

This clearly shows the proposal does not meet the principle of *horizontal equity* which is a long-standing tax policy principle accepted by governments. Broadly, the principle is that

[34] See Budget Paper 2, page 44.
[35] See Budget Paper 2, page 44.

investors should bear the same tax burden regardless of whether they invest directly or indirectly. The proposed measure runs counter to this principle.

11.1.1 Example

Another example is shown below.

Where a MIT / AMIT derives a $100 discount capital gain, but has expenses of $20 that are to be allocated against the capital gain, the difference in the trust net income would be as follows:

Trust level	Current	Proposed
Discount capital gain	100	100
50% discount	50	-
Net gain	**50**	**100**
Expenses	-20	-20
Net income	***30***	***80***

Once the net income is distributed, the impact on an individuals' investor's taxable income could be illustrated as follows (with direct investment included for comparison):

	Invest through MIT/AMIT		Direct investment
Individual level	Current	Proposed	
Distribution	30	80	100
Gross up	30	-	-
Gross gain	**60**	**80**	**100**
1/2 discount	-30	-40	-50
Individual expenses	**-**	**-**	**-20**
Taxable income	***30***	***40***	***30***

The example above equally applies if fund-level expenses are replaced by carry forward revenue losses.

The examples above and in Attachment F show where expenses or carry-forward revenue losses are offset against these discount capital gains at the MIT / AMIT level, the proposed measure will result in members that are entitled to discounting (individuals, complying superannuation funds entities and trusts taxed under Division 6) being worse off under this proposal than if they had invested in assets directly under the same scenario.

11.1.2 Discussion

The current CGT treatment does not always achieve parity between direct investment and investment through a MIT/AMIT; but the proposed change does not achieve this parity either — and for most investors the change moves the treatment further away from parity.

The FSC submits that, across the investment life-cycle of a managed fund, many (perhaps nearly all) AMITs and MITs would allocate expenses, or current year or carry forward revenue losses, against capital gains. This means that the proposed measure will disadvantage many or all AMITs and MITs relative to direct investment by individuals and superannuation funds.

The proposal also introduces another inconsistency: Division 6 trusts would be able to access the CGT discount, while MITs and AMITs will not. The FSC submits this is inconsistent and confusing and further underlines the concern that this proposal is clearly not meeting the policy intent of ensuring direct and indirect investment is treated similarly.

Another issue will emerge if the proposal is implemented. The allocation of expenses against different types of income has not been definitively addressed since the repeal of section 50 of the Income Tax Assessment Act 1936. That section prescribed an order for the allocation of expenses and was particularly relevant in the context of the former Undistributed Profits tax. Since the repeal there have been miscellaneous rulings and statements to the effect that direct expenses should be allocated to the income to which they relate but that general and surplus direct expenses should be allocated pro rata against taxable income. Whether this is correct and whether any gross or discounted capital gains should form part of this allocation base is an issue that until this proposal did not matter. However, the change, as it is proposed, will force the Government to deliberate and prescribe an outcome. Such an outcome will inevitably have consequences beyond MITs and AMITs.

We note the original exposure drafts of the AMIT legislation included this measure, but it was removed by Treasury during consultation. We understand this change was made because of the concerns raised above in this paper: disallowing the CGT discount at the trust level reduced tax neutrality compared to direct investment.

Given the increased compliance costs from the measure and the distortion in the tax treatment of direct vs indirect investment, the proposed CGT change would likely actively discourage many investors (individuals and superannuation funds) from investing in MITs and AMITs, adding to the competitiveness issues raised earlier in this submission.

The added burden on MITs and AMITs caused by higher taxation and higher compliance costs from these combined proposals means the benefit of reforming and moving out of Division 6 has been considerably reduced — possibly negated. It also is particularly concerning that this change has been proposed after many fund trustees have made the irrevocable election to adopt the AMIT regime.

We note that this measure is ostensibly meant to prevent beneficiaries that are not entitled to the CGT discount from getting a benefit from the CGT discount being applied at the trust level. This would be non-resident investors and corporate investors.

It is not clear why the Government has proposed a measure targeting all investors in AMITs and MITs rather than a measure specifically targeting resident corporations and non-resident beneficiaries. Instead, the Government proposes a measure that will result in individuals and superannuation funds paying an inappropriate amount of tax compared to direct investment.

Additionally, the beneficiaries of apparent concern represent a small proportion of unitholders. According to the ABS, non-government trading companies represent just 1.85% of total investment into managed funds, and foreign investors represent 5.8% of total investment.[36] Most investment is by individuals, superannuation funds and pension funds. In addition, capital gains are only subject to tax for non-residents when the gains relate to "taxable Australian Real Property" (**TARP**). Other gains are not subject to Australian tax. Hence the supposed mischief relates to a small proportion of the total gains recorded by the fund.

If the Government wishes to address concerns about corporates and non-residents accessing the CGT discount through MITs and AMITs, then we submit there would be value in exploring options that are more targeted at the issue. The FSC has provided a range of options to Treasury and we are willing to discuss these options in more detail. We await further consideration of these options.

Instead of this measure, the FSC is recommending a measure targeted at corporates and non-residents that are accessing the CGT discount through MITs and AMITs.

11.2 Proposed changes to attribution penalties for managed funds

The draft legislation to implement the Corporate Collective Investment Vehicle (CCIV) released in early 2019 contained the proposal for an extension of the penalty for attribution 'unders and overs' that result from a lack of reasonable care. This change will apply both to the new CCIV investment vehicle as well as an existing funds management vehicle, Attribution Managed Investment Trusts (AMITs).

FSC members completely oppose this change. If this penalty remains in the final legislation, it will prove to be a significant disincentive for any fund manager to elect into the CCIV (or AMIT) regime for its funds.

The change in the penalty regime for AMITs was a deliberate decision as part of the AMIT consultation process. Early exposure drafts of the AMIT Regime legislation included administrative penalties relating to 'unders and overs' where there had been a lack of reasonable care. However, this was removed as part of the consultation process in recognition of stakeholder concern about the application of the reasonable care concept.

The absence of the reasonable care requirement in the AMIT rules was not an 'oversight' that requires correction. It was a deliberate change based upon consultation on that point, recognising commercial factors particular to the industry. Changing the penalty regime for the CCIV and AMIT regime without evidence of the need for this requirement would be ignoring this consultation.

We also note the alleged mischief from attribution 'unders and overs' is negligible. AMITs and CCIVs are, in general, not meant to be taxpaying entities; and any unders or overs would be expected to largely cancel out over time. As a result, the amount of tax at risk over time is very small.

[36] ABS Managed Funds, September 2018, table 9.

Penalties in the tax system should be proportionate – an approach that should apply across all government policy. However, in this case, proportionality does not apply. A potentially substantial penalty is being applied in relation to a negligible tax liability.

The non-zero risk of a reasonable care penalty will be a further discouragement from foreign investors using CCIVs and AMITs compared to other international vehicles, particularly vehicles in the Asia Region Funds Passport. For Australian taxpayers, it will discourage the use of CCIVs and AMITs compared to other vehicles such as Listed Investment Companies (LICs) and non-AMIT trusts.

We understand the main argument in favour of the proposed change is that it will mean the same tax penalty regime will apply to all Australian taxpayers. However, this argument is without substance:

- AMITs and CCIVs could be penalised for attributing *too much* assessable income to investors. It appears CCIVs and AMITs would be the only classes of taxpayer subject to reasonable care penalties where there has been no tax shortfall. If the goal is to be consistent, then this would lead to another impractical conclusion: penalties should apply to *all* taxpayers who pay too much tax (a conclusion that fund managers would oppose).
- AMITs currently have (and CCIVs will have) substantially different administrative rules for income tax compared to other taxpayers. In particular, other taxpayers (in general) do not use estimates to calculate taxable income in one tax period and then 'true up' the estimates in a later period.[37]
    - Other taxpayers could be penalised for using this approach as they are not permitted to use 'unders and overs' that is central to the attribution system. Again, if the goal is for the administration of income tax to be consistent across all taxpayers, then this would lead to the impractical conclusion that *no* taxpayers should be able to use 'unders and overs' (again, a conclusion that fund managers would naturally oppose).

The points above lead to the conclusion that AMITs and CCIVs *are* different from other taxpayers – and so therefore the consistency argument for penalties fails.

We also note the following:

- Evidence has not been presented showing the current approach, involving penalties for errors due to recklessness alone, is not working adequately.
- It has not been shown that the addition of this new penalty is of net benefit, noting the costs of the new penalty system, including added costs and uncertainty.
- The proposal will strongly discourage investment into assets that are more likely to produce 'unders and overs' such as property. Investment managers may just not want the risk of being confronted with a penalty for using the 'unders and overs' provisions.

[37] Taxpayers can amend earlier year returns, but this is quite different from carrying forward the differences between estimated and actual figures and offsetting these against future year returns.

- the ATO has released guidance on acceptable practice for making attribution estimates for AMITs.[38] If the threshold for AMIT penalties is lowered, then either:
    - the ATO guidance will change, in which case the law change will trap otherwise acceptable AMIT practices, highlighting the FSC concerns raised above; or
    - the ATO guidance will not change, in which case it is unclear why the law change was required.

We also strongly object to the retrospective nature of this proposal on MITs that have already elected into the AMIT regime and are unable now to exit this regime due to the irrevocable election made at the time. Arguably, there would not be a retrospective element to the proposal if AMITs were able to exit the regime, but the fact that there is no possibility of exit means the proposed penalty change operates to some extent retrospectively on AMITs that are now in the regime.

Furthermore, if MIT operators had the benefit of hindsight that the reasonable care test would be inserted at a later date, then it would have been a significant factor impacting the decision to elect into AMIT. Changing the penalty regime after the decisions is moving the goalposts after the game has started.

Therefore, if the change in the penalty regime is retained in the final CCIV legislation, then the FSC recommends that AMITs be provided with the option to leave the attribution regime to ensure the retrospective element of the proposal is removed.

[38] ATO LCR 2015/10 Attribution Managed Investment Trusts: administrative penalties for recklessness or intentional disregard of the tax law - section 288-115 See: https://www.ato.gov.au/law/view/document?DocID=COG/LCR201510/NAT/ATO/00001&PiT=99991231235958