EXPLANATORY STATEMENT

Issued by authority of the Assistant Treasurer and Minister for Financial Services

Income Tax (Transitional Provisions) Act 1997

Income Tax (Transitional Provisions)(Permanent Incapacity Benefits) Amendment Rules 2024

Section 301-105 of the *Income Tax (Transitional Provisions) Act 1997* (the Act) provides that the Minister may, by legislative instrument, make rules prescribing matters of a transitional nature (including prescribing any saving or application provisions) that:

- relate to the amendments or repeals made by Schedule 9 to the *Treasury Laws Amendment (2022 Measures No. 4) Act 2023*; and

- relate to either or both of the 2022-23 and 2023-24 income years.

The purpose of the *Income Tax (Transitional Provisions) (Permanent Incapacity Benefits) Amendment Rules 2024* (the Rules) is to continue transitional arrangements made by section 301-100 of the Act for another 12 months to include the 2023-24 income year.

Section 301-100 of the Act prevents the Commissioner from amending certain income tax assessments on the basis that a superannuation benefit paid to a person is a superannuation income stream benefit because of amendments made by Schedule 9 to the *Treasury Laws Amendment (2022 Measures No. 4) Act 2023* ('the Schedule 9 amendments'). Those amendments reversed the effect of the Federal Court's decision in *Commissioner of Taxation v Douglas* [2020] FCAFC 220 (the Douglas decision) by clarifying that all defined benefit pensions paid from most defined benefit funds (including permanent incapacity benefits) are superannuation income stream benefits and not superannuation lump sums for the purpose of the *Income Tax Assessment Act 1997*.

Section 301-100 of the Act is a transitional arrangement that applies for income years up to and including the 2021-22 income year. The *Income Tax (Transitional Provisions) (Permanent Incapacity Benefits) Rules 2024* (made under section 301-105 of the Act) provide equivalent treatment for the 2022-23 income year. Section 301-100 of the Act applies to certain recipients of permanent incapacity benefits who had previously had their superannuation benefits assessed on the basis that they were a superannuation lump sum, and this assessment was first made before 4 December 2020 (the date of the Douglas decision). In practice, this means taxpayers whose superannuation benefits commenced before the 2020-21 income year, as benefits commencing in the 2020-21 income year will not have the relevant assessment made before 4 December 2020.

The Rules apply to income tax assessments for the 2023-24 income year.

The Rules extend the transitional arrangements for a further year. This will provide relevant funds and individuals with further time to transition some aspects of reporting the incapacity benefits as superannuation lump sums to reporting them as superannuation income streams. The Rules mean that if the Commissioner makes an assessment on the basis that a permanent incapacity benefit is a superannuation lump sum for the 2023-24

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income year, the Commissioner is prevented from amending that assessment to assess the benefit as a superannuation income stream benefit if it meets the conditions set out in the Rules. However, the Commissioner may amend the assessment for reasons such as fraud or dishonesty, or if the taxpayer requests a review of the assessment.

The Act specifies conditions that need to be satisfied before the power to make the Rules may be exercised. As outlined above, the Minister can only make rules dealing with transitional arrangements in relation to the Schedule 9 amendments and only for the 2022-23 and 2023-24 income years. These regulations meet those conditions.

The Rules also meet the condition in subsection 301-105(3) of the Act, which provides that the rules must not create an offence or civil penalty, provide coercive powers, impose a tax, set an amount to be appropriated or directly amend the text of the Act.

The decision to extend the transitional arrangements for the 2023-24 income year was based on feedback from relevant superannuation funds indicating that they required additional time to fully transition to the new law. Those funds were advised of the Minister's intent to make Rules to extend the transitional arrangements for the 2023-24 year. Formal consultation was not undertaken on the draft instrument as the Rules simply extend existing transitional arrangements that are already understood by those funds. As the Rules apply in relation to a past income year, making the Rules promptly will provide certainty to relevant taxpayers.

The Rules are a legislative instrument for the purposes of the *Legislation Act 2003*, and are subject to disallowance and sunsetting in accordance with that Act.

The Rules commenced on the day after registration.

The Rules apply retrospectively in relation to the 2023-24 income year. It is appropriate to extend the transitional arrangements for a further year to provide additional time for relevant funds and individuals to make the transition. The Rules will not have any detrimental impacts on individual taxpayers and therefore are not affected by subsection 12(2) of the *Legislation Act 2003*. The Rules will preserve assessments that are made in relation to the 2023-24 income year, providing greater certainty for taxpayers.

Details of the legislative instrument are set out in <u>Attachment A</u>.

A statement of Compatibility with Human Rights is at <u>Attachment B.</u>

The Office of Impact Analysis has been (OIA) has been consulted and agreed that an Impact Analysis is not required.

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ATTACHMENT A

Details of the *Income Tax (Transitional Provisions) (Permanent Incapacity Benefits) Amendment Rules 2024*

Section 1 – Name

This section provides that the name of the regulations is the *Income Tax (Transitional Provisions) (Permanent Incapacity Benefits) Amendment Rules 2024* (the Rules).

Section 2 – Commencement

The Rules commenced on the day after the instrument is registered on the Federal Register of Legislation.

Section 3 – Authority

The Regulations are made under the *Income Tax (Transitional Provisions) Act 1997* (the Act).

Section 4 – Schedule

This section provides that each instrument that is specified in a Schedule to this instrument is amended or repealed as set out in the applicable items in the Schedule, and any other item in the Schedule to this instrument has effect according to its terms.

Schedule 1 – Amendments

Item 1 makes a consequential amendment to the heading to section 5 of the Rules to signal that the existing section 5 of the *Income Tax (Transitional Provisions) (Permanent Incapacity Benefits) Rules 2024* deals with transitional arrangements for assessments for the 2022-23 income year.

Item 2 inserts a new section 6 into the Rules, which sets out the transitional arrangements for assessments for the 2023-24 income year. The conditions for the transitional arrangements to apply are consistent with the transitional provisions in section 300-100 of the Act. That is:

- a superannuation benefit (the trigger benefit) was paid to the person in the 2020-21 income year or an earlier income year; and
- the Commissioner made an assessment for the income year for the individual before 4 December 2020; and
- the trigger benefit was paid to the individual because the individual satisfied a condition of release specified in item 103 (permanent incapacity) of the table in Schedule 1 to the Superannuation Industry (Supervision) Regulations 1994; and
- the Commissioner made the assessment on the basis that the trigger benefit was a superannuation lump sum.

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If the above conditions are met, the Rules prevent the Commissioner from amending an assessment for the 2023-24 income year, to assess a superannuation benefit as a superannuation income stream benefit, in the following circumstances:

- the superannuation benefit was paid to the individual because the individual satisfied a condition of release specified in item 103 (permanent incapacity) of the table in Schedule 1 to the *Superannuation Industry (Supervision) Regulations 1994*; and
- the Commissioner made the assessment on the basis that the superannuation benefit was a superannuation lump sum; and
- the Commissioner also made an assessment for the 2022-23 income year on the basis of the benefit being paid for permanent incapacity and on that basis that it was a superannuation lump sum.

The effect of this provision is to facilitate continuing transitional treatment of certain permanent incapacity superannuation benefits that had previously been treated as superannuation lump sums prior to the Douglas decision. It will only apply where that transitional lump sum treatment was applied in 2022-23, ensuring that the Rules are appropriately targeted only to those funds and permanent incapacity benefits that have not yet fully transitioned to the new arrangements.

Consistent with the Act, the Rules clarify that the Commissioner may amend an assessment for other reasons, such as fraud or evasion or review and appeal.

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ATTACHMENT B

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

Income Tax (Transitional Provisions) (Permanent Incapacity Benefits) Amendment Rules 2024

This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Legislative Instrument

The purpose of the *Income Tax (Transitional Provisions) (Permanent Incapacity Benefits) Amendment Rules 2024* (the Rules) is to continue transitional arrangements made by section 301-100 of the *Income Tax (Transitional Provisions) Act 1997* (the Act) for a further 12 months to include the 2023-24 income year.

Section 301-100 of the Act prevents the Commissioner from amending certain income tax assessments on the basis that a superannuation benefit paid to a person is a superannuation income stream benefit because of amendments made by Schedule 9 to the *Treasury Laws Amendment (2022 Measures No. 4) Act 2023* ('the Schedule 9 amendments'). Those amendments sought to reverse the effect of the Federal Court's decision in *Commissioner of Taxation v Douglas* [2020] FCAFC 220 (the Douglas decision) by clarifying that all defined benefit pensions paid from most defined benefit funds (including permanent incapacity benefits) are superannuation income stream benefits and not superannuation lump sums for the purpose of the *Income Tax Assessment Act 1997*.

Section 301-100 of the Act is a transitional arrangement that applies for income years up to and including the 2021-22 income year. The *Income Tax (Transitional Provisions) (Permanent Incapacity Benefits) Rules 2024* (made under section 301-105 of the Act) provide equivalent treatment for the 2022-23 income year. Section 301-100 of the Act applies to certain recipients of permanent incapacity benefits who had previously had their superannuation benefits assessed on the basis that they were a superannuation lump sum, and this assessment was first made before 4 December 2020 (the date of the Douglas decision). In practice, this means taxpayers whose superannuation benefits commenced before the 2020-21 income year, as benefits commencing in the 2020-21 income year will not have the relevant assessment made before 4 December 2020.

The Rules extend the transitional arrangements for a further year to cover the 2023-24 income year. This will provide relevant funds and individuals with further time to transition some aspects of reporting the incapacity benefits as superannuation lump sums to reporting them as superannuation income streams. The Rules mean that if the Commissioner makes an assessment on the basis that a permanent incapacity benefit is a superannuation lump sum for the 2023-24 income year, the Commissioner is prevented from amending that assessment if it meets the conditions set out in the Rules. However, the Commissioner may amend the assessment for reasons such as fraud or dishonesty, or if the taxpayer requests a review of the assessment.

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Human rights implications

This Legislative Instrument does not engage any of the applicable rights or freedoms.

Conclusion

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.

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