AUSTRALIAN JUDICIAL OFFICERS ASSOCIATION

AJOA Submission to the Senate Economics Legislation Committee on the Treasury Laws Amendment (Better Targeted Superannuation Concessions and Other Measures) Bill 2023 and the Superannuation (Better Targeted Superannuation Concessions) Imposition Bill 2023

23 February 2024

1 The Australian Judicial Officers Association (**AJOA**) appreciates the opportunity to make submissions concerning the *Treasury Laws Amendment* (*Better Targeted Superannuation Concessions and Other Measures) Bill 2023* (the **Bill**) and *Superannuation (Better Targeted Superannuation Concessions) Imposition Bill 2023* (the **Imposition Bill**) (together, the **Bills**).

2 Membership of the AJOA is open to all serving and retired judges and magistrates in Australia. The membership of the AJOA currently stands at 921 (which includes 60% of current judicial officers in Australia). The AJOA's objects are concerned with the public interest in maintaining a strong and independent judiciary within a democratic society that adheres to the rule of law.

3 The Bills propose that from 2025/26, under Div 296 of the *Income Tax Assessment Act 1997* (Cth) (**ITAA 1997**), an individual taxpayer with a "total superannuation balance" exceeding $3 million will be liable to tax (**Div 296 tax**) in respect of the taxpayer's "taxable superannuation earnings" at the rate of 15%. The tax is to be imposed directly on the individual.

4 The AJOA has profound concerns about the proposed application of Div 296 tax to pension entitlements of Commonwealth and Territory judges (identified in para 8) under statutory pension schemes (**Statutory Pension Entitlements**) and opposes the proposed amendments. The AJOA also proposes to make submissions concerning the position of State judges (identified in para 8) following the release of proposed regulations defining "State higher level office holders" and related aspects of the proposed legislative scheme.

5 Statutory Pension Entitlements are already subject to the highest marginal tax rate

of 45% plus Medicare levy of 2% when paid. In that respect, Statutory Pension Entitlements are fundamentally different from the superannuation funds which are the principal target of the Bills. The proposed Div 296 tax would impose a substantial additional tax upon the Statutory Pension Entitlements of Commonwealth and Territory judges.

6 In summary, the AJOA submits that the proposed application of Div 296 tax to Commonwealth and Territory judges' Statutory Pension Entitlements would produce inequitable outcomes and be contrary to the public interest. That is so for the following reasons:

(1) The application of Div 296 tax to Commonwealth and Territory judges would undermine a fundamental rationale for such entitlements, namely the preservation of the independence of the judiciary, and would accordingly be contrary to the public interest. The minor fiscal benefit to the Commonwealth cannot justify such erosion of Australia's system of democracy.

(2) The differential application of the proposed Div 296 tax as between State judges and Commonwealth and Territory judges will have significant corrosive consequences for the judicial system in Australia.

(3) The differential application of the proposed Div 296 tax between different categories of Commonwealth judges (depending on their dates of appointment) will also have adverse impacts upon the judicial system.

(4) Div 296 tax would create adverse consequences in terms of addressing the gender disparity in the composition of the Commonwealth and Territory courts.

(5) The design of the proposed Div 296 tax proceeds from a false premise that: (a) a Statutory Pension Entitlement is economically equivalent to an interest in a superannuation fund; and (b) the existing taxation treatment of a Statutory Pension Entitlement is equivalent to the existing taxation treatment of income arising in a private sector superannuation fund and pensions and withdrawals from such funds. Consequently, the impact of the

proposed Div 296 tax will, with few exceptions, result in a much higher overall level of taxation on the pensions of Commonwealth and Territory judges (and others entitled to statutory defined benefit pensions) than would be imposed on any other income derived by any other taxpayer. As a matter of tax policy and design and equity, this discriminatory outcome is unjustifiable.

(6) Retired judges would be particularly disadvantaged because pensions paid to retired judges would be taxed more heavily than any other form of income or profits.

(7) The proposed Div 296 tax is likely to be unconstitutional in its application to current and retired Commonwealth judges. It is undesirable to enact taxation laws which are so uncertain in their operation and legality.

(8) Current Territory judges will be treated even more disadvantageously than current Commonwealth judges because they would immediately be affected by Div 296 tax. This will undermine democracy and self-government in the Territories, as well as the institutional integrity of the Territory Supreme Courts.

7 These submissions will address each of these matters in detail.

Overview of the Bills

8 There are special provisions proposed for working out Div 296 tax in respect of Statutory Pension Entitlements for the following categories of judicial officers:

- "State higher level office holders" to be prescribed by regulation, but whom it is assumed will include at least judges of the State Supreme Courts and County or District Courts in respect of interests in "constitutionally protected funds" (**State judges**); and
- currently serving judges of the High Court of Australia, the Federal Court of Australia and the Federal Circuit and Family Court of Australia (Division 1) (**Commonwealth judges**) in respect of interests under the *Judges' Pension Act 1969* (Cth) (the ***Judges' Pension Act* (Cth)**).

9 The effect of the Bills on State, Commonwealth and Territory judges would be (in summary):

- For all such judges, the notional capital value of their Statutory Pension Entitlements would be aggregated with their private superannuation entitlements in determining their "total superannuation balance" to determine if the balance exceeds the $3 million threshold; and, if it does, Div 296 tax would be imposed on "earnings" in respect of any private superannuation interests.
- For State judges, Div 296 tax would not be imposed on "earnings" in respect of superannuation interests in constitutionally protected funds.
- For Commonwealth judges:
  (a) Div 296 tax would not apply to "earnings" in respect of accruing pension entitlements under the *Judges' Pension Act* (Cth) of currently serving Commonwealth judges who were appointed prior to 1 July 2025;
  (b) Div 296 tax would apply to "earnings" in respect of pension entitlements of currently serving Commonwealth judges who were appointed prior to 1 July 2025, once they retire;
  (c) Div 296 tax would apply to "earnings" in respect of accruing pension entitlements of Commonwealth judges appointed from 1 July 2025 while they are serving (but will not be payable until they retire) and will also apply to "earnings" in respect of pension entitlements after they retire; and
  (d) Div 296 tax would apply to "earnings" in respect of pension entitlements of already retired Commonwealth judges.
- For all Territory judges, current, future and retired, Div 296 tax would apply in respect of all of their pension entitlements as per (c) and (d) above, regardless of the dates of their appointment.

10 The "earnings" in respect of which Div 296 tax would be imposed are to be calculated by reference to changes in the "total superannuation balance" of a

judge's Statutory Pension Entitlement. The "total superannuation balance" of such a "superannuation interest" at a particular time is to be determined in accordance with regulations (not yet published). It is assumed that the "total superannuation balance" of such an entitlement, under the *Judges' Pension Act* (Cth) (and its State and Territory equivalents) will be the actuarially determined value of that entitlement at a particular time.

Application of Div 296 tax to Commonwealth and Territory judges would undermine the independence of the judiciary and would be contrary to the public interest

11 It is understandable that the Bills aim to raise revenue and, to that end, intend to hit as wide a target as possible. However, consideration must be given to the role of judges in our system of democracy and the rationale for all legislatures having enacted legislation providing for non-contributory pensions for judges.

12 In *State Chamber of Commerce & Industry v Commonwealth* (1987) 163 CLR 329, Brennan J observed at (362)-(363) that the existence and nature of government depends upon the performance of the essential organs of government, including the courts, and in that regard emoluments have an important role.

13 In *Austin & Anor v Commonwealth* (2003) 215 CLR 185, Gaudron, Gummow and Hayne JJ observed at [167]:

> The circumstances that judicial pensions do not require contributions but are fixed as a proportion of the remuneration of a serving judge and are to be paid at the full rate only upon a substantial period of service as well as attainment of a minimum age, indicates the importance attached by legislatures to such schemes in the remuneration of the judicial branch.

14 The importance attached by State, Commonwealth and Territory legislatures to judicial pension schemes is founded in the necessity for an independent judiciary. In *Forge v Australian Securities and Investments Commission* (2006) 228 CLR 45 Gummow, Hayne and Crennan JJ explained at [76]-[77]:

> Further, if attempting to state comprehensively the measures that have been taken to support judicial independence, it would be necessary to take account of not only the arrangements for remuneration of judges while in

> office but also the provision made for payment of pensions on retirement. The "remuneration", which s 72(iii) of the Constitution states shall not be diminished during continuance in office, includes non-contributory pension plan entitlements which accrue under the federal judicial pensions statute.
>
> Provision is made for judicial pensions for a number of reasons. One not insignificant reason is to reduce, if not eliminate, the financial incentive for a judge to seek to establish some new career after retirement from office. As was pointed out in argument, it may otherwise be possible to construe what a judge does while in office as being affected by later employment prospects.

15 In *Baker v Commonwealth* (2012) 206 FCR 229, Keane CJ and Lander JJ observed at [37] in respect of s 72(iii) of the Constitution:

> …[A]s a matter of history, the principal vice at which this provision was aimed was the legislative reduction in judicial remuneration, after a judge had accepted appointment. Such a reduction was viewed as a means of punishing an independently minded judge or of ensuring a more compliant or cooperative attitude on the part of serving judges in the execution of their function as the third branch of government.

16 The role of judicial pensions in the reality and perception of judicial independence is reflected in the *Guide to Judicial Conduct* issued by the Chief Justices of Australia which states:

> The benefits of office including pensions or superannuation, should give a comfortable level of financial security for life to obviate the need to augment earnings by activities that might generate a conflict of interest or otherwise pose a potential threat to public confidence.

17 Judges, by convention, voluntarily limit their sources of income in order to preserve their independence and the public perception of their independence. The proposed application of Div 296 tax in respect of judges' pensions is likely to have detrimental effects upon both the independence and quality of the Commonwealth and Territory judiciary. First, it would encourage judges to look towards future sources of earnings after retirement, thereby eroding the independence or perceived

independence of the judiciary. Secondly, persons who would make exemplary judges may reject judicial office in favour of the opportunity to earn more elsewhere and also to avoid the substantial impact of Div 296 tax which, in due course, would create an impact which could not otherwise be avoided as a judge's Statutory Pension Entitlement is not commutable. In either case, there would be institutional damage to the courts.

18 Thus, the implications of reduction of judicial Statutory Pension Entitlements, through taxation or otherwise, are not merely fiscal, but necessarily involve broader issues concerning the effect upon our system of democracy and government. While, taking a short-sighted view, the application of the proposed Div 296 tax to judges' Statutory Pension Entitlements would marginally increase revenue, it will have a broader detrimental consequence on the institutions of our democracy.

The differential application of the proposed Div 296 tax as between State judges and Commonwealth and Territory judges will have significant corrosive consequences for the judicial system in Australia.

19 If the proposed changes are made, they will operate differentially between State judges, Commonwealth judges and Territory judges.

20 This will have the unintended effect of making an appointment to a State Supreme Court a financially more attractive proposition than appointment to the Federal Court or Territory courts, with the following consequences:

- First, many experienced, skilled, and talented lawyers will choose appointment to State courts over Commonwealth and Territory courts.
- Secondly, some persons in private practice are likely to decline judicial appointment, even to the High Court.
- Thirdly, some judges of Commonwealth and Territory courts are likely to move to State courts, causing a drain of talent.

21 Consequences of this kind are not merely speculative but are demonstrated by history. The legislation considered in *Austin & Anor v Commonwealth*, which introduced a superannuation contributions surcharge for judges' pensions, continued to apply to Commonwealth judges. There are well-known examples of

talented judges who left Federal courts for State courts as a result. Division 296 tax would operate to dilute the quality of Commonwealth and Territory courts in favour of State courts when it is desirable to maintain parity of quality between the courts.

22 This will adversely affect Commonwealth and Territory courts and, indeed, the Commonwealth and the Territories themselves. It would be contrary to the public interest for the courts responsible for administering Commonwealth and Territory laws to become regarded as second-rate in comparison to State Courts.

23 The number of Commonwealth judges whose judicial pensions would be inequitably affected by Div 296 tax in comparison to their State counterparts bears examination. There are 95 current Commonwealth judges who would be affected (High Court, Federal Court and FCFCOA (Div1)). In comparison, there are approximately 438 State judges (Supreme and District or County Courts) whose pensions would be unaffected by Div 296 tax (except as described in the first dot point of para 9). It can be expected that there are comparable proportions of retired Commonwealth judges whose pensions would be affected.

24 Two points should be made about these numbers. First, they demonstrate that the revenue that would be raised from current and retired judges would be relatively small, particularly when weighed against the substantial public interest and constitutional and other detriments that would flow. Secondly, they demonstrate that the vast majority of judges in Australia would not have their pensions affected by Div 296 tax, emphasising the discrepancy and inequality between the proposed treatment of a relatively small cohort of Commonwealth judges, on the one hand, and their State peers on the other.

The differential application of the proposed Div 296 tax between different categories of Commonwealth judges will also have adverse impacts upon the judicial system

25 Division 296 tax is proposed to be imposed on “earnings" in respect of the pension entitlements of Commonwealth judges appointed from 1 July 2025, even during the period when they are serving. There will be differential treatment of newly appointed judges in comparison to already serving judges.

26 The proposed differentiation has the potential to create division within the cohort of judges in the respective Commonwealth courts. Such differentiation may cause a perception that there are two classes of judges hearing the same kinds of matters. Such a perception would be detrimental for the reputation of the courts and respect for the rule of law. It is unthinkable, for example, that the judges of the High Court, sitting on the same cases, should receive different levels of net remuneration (the judicial pension being, as has been emphasised, part of a judge’s remuneration).

27 There is an important public interest in ensuring that all judges within the same division of a court are, and are perceived to be, equal.

Adverse consequences in terms of addressing the gender disparity in the composition of the Commonwealth and Territory courts

28 Women are represented on superior courts in, generally speaking, significantly lower numbers than on inferior courts. Specifically, in relation to Federal courts: only 37.5% of the judges on the Federal Circuit and Family Court of Australia are female and only 31.5% of the judges on the Federal Court of Australia are female.

29 For a number of reasons, the proposed Div 296 tax would have a potentially disproportionate adverse impact on female candidates and on current and retired female judges, and thereby be corrosive of efforts to ensure greater female representation on Federal superior courts.

30 First, female barristers appointed to judicial office (past, present and future) are likely to have accumulated less in assets than their male counterparts, thereby amplifying the impact of a substantial tax payment at retirement based on their notional pension earnings. This is a consequence of the historical discrepancy between the earnings of male and female barristers in Australia, which continues

to the present day. This is demonstrated in, for example, the *Law Council of Australia, Equitable Briefing Policy Annual Report: 2022-2023 Financial Year.* The Law Council further notes that, "the data about the remuneration of barristers that is publicly available, such as that published by the ATO, suggests a gender pay gap at the Australian Bar that is significantly higher than Australia's total remuneration gender pay gap of 22.8%." Additionally, women tend to take longer periods of unpaid parental leave.

31 Secondly, an actuarial assessment of the total superannuation balance value for the purposes of Div 296 tax for women judges will likely exceed that of their male counterparts because of the greater life expectancy rates for women in Australia.

32 Thirdly, there is a tendency to offer appointments to outstanding female candidates at an earlier age than male candidates, as one means by which to address the historical gender disparity on superior courts. However, this means that women appointed after 1 July 2025 or on Territory courts would, if they accept early appointment, accrue Div 296 tax for a longer period of time resulting in a greater tax liability on retirement.

33 Cumulatively, these factors mean that female candidates and female judges (including retired female judges) are likely to have fewer assets than their male counterparts while being exposed to a potentially greater tax on their notional judicial pension earnings. This difficulty would be particularly acute in the case of female judges appointed to Commonwealth courts after 1 July 2025 and female judges appointed to Territory courts.

34 The result is that Div 296 tax may have a disproportionately adverse impact on women. This in turn may operate as a powerful disincentive for women in particular to accept judicial appointment to Commonwealth and Territory courts, and may provide a particularly strong incentive for serving female judges on such courts to transfer to State courts.

The impact of the proposed Div 296 tax will (with few exceptions) result in a much higher overall level of taxation for Commonwealth and Territory judges than would be imposed on any other income derived by other taxpayers

35 While it may have been thought that the application of Div 296 tax to judges' Statutory Pension Entitlements is consistent with an announced policy objective of ensuring that defined benefit interests are accorded commensurate treatment to account-based superannuation funds, the premise underlying that approach is false, for two reasons.

36 First, unlike private superannuation funds, judges' Statutory Pension Entitlements do not allow for the personal accumulation of funds in a concessional tax environment which can later be cashed out or bequeathed to family members. It follows that a major policy reason for introducing the proposed Div 296 tax – to counter the exploitation of tax preferences in the superannuation system for the purposes of wealth accumulation in excess of that required for a "dignified retirement"[1] – simply does not apply in the case of judges' Statutory Pension Entitlements.

37 Secondly, judges' Statutory Pension Entitlements are not a superannuation fund as that expression is ordinarily understood. Judges make no contributions to any such fund for their benefit. However, the Bills construct a notional scheme under which Statutory Pension Entitlements are taxed as if such contributions are made.

38 Thirdly, there are fundamental differences between the way in which a pension paid to a judge is currently taxed, and the way in which income and gains in private sector complying superannuation funds and distributions from such funds to members, are currently taxed. The design of the proposed Div 296 tax ignores this fundamental distinction and therefore produces completely inequitable tax outcomes.

39 In order to illustrate this point, we first summarise the way in which the proposed Div 296 tax would apply alongside the existing tax regime for private account-based superannuation arrangements. We then summarise the way in which the proposed Div 296 tax would apply alongside the existing tax regime for pensions

[1] Para 1.11 of the Explanatory Memorandum to the Bills.

paid to judges.

The effect of the proposed Div 296 tax on individuals with account-based superannuation arrangements

40 An individual member of a private sector complying superannuation fund currently benefits from the following considerable tax advantages:

- during the accumulation phase, a maximum tax rate of 15% on income within the fund and 10% on capital gains for assets held for at least 12 months;
- during the retirement phase, a zero tax rate on fund income and gains relating to the investment of funds supporting a pension; and
- during the retirement phase, a zero tax rate on any pension paid by the superannuation fund or withdrawal of the accumulated funds from the age of 60.

41 The aim of the proposed Div 296 tax is to limit those tax advantages to some extent but not eliminate them.[2] Where an individual member has accumulated a balance of more than $3 million in one or more private sector account-based superannuation arrangements, the member would be liable to pay Div 296 tax at 15% in respect of "earnings" in the superannuation funds to the extent that the "earnings" relate, arithmetically, to accumulated funds that exceed $3 million at the end of the income year. However, **the existing favourable tax regime would continue to apply** in parallel with the Div 296 rules. A maximum tax rate of 15% would continue to apply to income on funds in a private sector complying superannuation fund. Pensions payable by the superannuation fund and withdrawals from the superannuation fund from the age of 60 would continue to be tax free. Consequently, in the context of the tax rules that apply to private account-based superannuation arrangements, Div 296 tax can legitimately be regarded as tempering the generosity of existing tax concessions.

[2] Paras 1.2 and 1.10 of the Explanatory Memorandum to the Bills.

The effect of the proposed Div 296 tax on pensions paid to judges

42 In contrast, under current tax law, a person (such as a judge) with a Statutory Pension Entitlement:

- obtains **no direct or indirect personal tax advantage** prior to retirement from the accumulation of funds in a tax-preferred environment; and
- after retirement is **fully taxed** at marginal income tax rates on the pension that is paid, subject only to a 10% annual tax offset (i.e tax credit) on the first $118,750 (currently) of the pension (i.e. a maximum offset of $11,875) after the age of 60.[3] In other words, the pension is taxed **in the same way as salary payments** except for the availability of a maximum annual tax offset which is currently $11,875. This tax treatment results from the pension being regarded for tax purposes as being paid from "untaxed funds". The premise on which the pension is fully taxed becomes unjustifiable if Div 296 tax is introduced.

43 Given the policy objective of Div 296 tax (i.e. to scale back the tax advantages available for superannuation), the only tax advantage in respect of a judge's Statutory Pension Entitlement that could legitimately be targeted by the proposed Div 296 rules would be the $11,875 maximum annual tax offset. But the proposed rules ignore the tax offset and instead seek to tax the notional growth of a balance on a notional superannuation account in respect of which a judge obtains no tax benefit and over which the judge has no control and which a judge may never receive. Unsurprisingly, the net tax position, in most cases, will be that Div 296 tax will exceed the pension tax offset that is available under the existing tax law, with the result that a judge will pay a higher rate of tax on retirement income than would be paid by any other taxpayer on any other income. This is clearly a discriminatory and unjust outcome.

44 The disjunction between the existing tax treatment of a judge's Statutory Pension Entitlement and the proposed Div 296 tax emerges starkly from the following estimates prepared by the AJOA on the basis of an actuarial opinion:

[3] Sections 303-3 and 303-4 of ITAA 1997. See further paras 46 and 47 below.

- For a Commonwealth judge appointed on or after 1 July 2025, the amount of Div 296 tax payable in the first year of retirement could be as high as 90% of the amount of the pension payable in that year.[4] In addition, income tax would be payable on the pension. Even if the average rate of income tax on the pension is as low as 35% (allowing for indexation of the existing tax offset), the total tax payable in the first year of retirement could be more than 125% of the amount of the judge's pension in the first year of retirement.

- Except in the case of some judges who have already retired, the amount of Div 296 tax payable annually by a retired Commonwealth judge would exceed the amount of the maximum tax offset under existing income tax law (allowing for indexation of the tax offset), resulting in a higher overall level of taxation than would be payable on salary. In one projection, the amount of Div 296 tax payable annually for a period of 21 years (excluding deferred Div 296 tax relating to the period before retirement) would exceed the amount of the indexed pension tax offset by an annual average of more than $27,000 (i.e. more than $565,000 over 21 years). This would represent a surcharge that is not payable by any other taxpayer on any form of income.

45 We submit that both of those outcomes are entirely unjustifiable from a tax policy perspective and as a matter of equity and fairness.

The approach taken in the Bill compared with the approach taken when the transfer balance cap rules were introduced

46 It is instructive to compare the design of the proposed Div 296 tax with the design of measures enacted in 2016 in Div 294 of ITAA 1997 (with effect from 1 July 2017) to limit the extent to which future income within a superannuation fund would be exempt from tax rather than being taxed at 15%. This purpose was achieved by limiting the amount of funds held by an individual within the

[4] This calculation is based on the conservative assumption that the Commissioner remits 100% of the interest charged on the deferred Div 296 tax under proposed s 135-65(2) of Schedule 1 to the *Taxation Administration Act 1953 (Cth)* (**Sch 1 TAA 1953**). Interest that is not remitted would be charged at the long term bond rate under proposed s 134-65(1) of Sch 1 TAA 1953, increasing the amount of the deferred liability.

superannuation system that could be transferred from an accumulation account to an account supporting the payment of a pension. The limit is referred to as the "general transfer balance cap". It was initially set at $1.6 million. As a result of statutory indexation, the cap is now $1.9 million.

47 In recognition of the fact that the tax treatment of defined benefit pensions is entirely different from the tax treatment of account-based pensions paid by superannuation funds, the Div 294 rules did not seek to impose a 15% tax on part of the actual or notional income in an actual or notional fund supporting a non-commutable defined benefit pension. Rather, Div 303 was introduced to restrict the concessional tax treatment available in respect of a defined benefit pension. For a defined benefit pension paid from an "untaxed fund" (such as a statutory defined benefit pension paid to a judge) to a person over the age of 60, the amount of a pension qualifying for a tax offset of 10% was limited to $100,000, producing a maximum annual tax offset of $10,000. This figure was chosen on the basis of an estimate that the "net present value of the additional lifetime tax paid by high balance accumulation members is estimated to be comparable to the net present value of the additional lifetime tax paid on unfunded defined benefit income over $100,000".[5] The "defined benefit income cap" has subsequently been increased to $118,750 through statutory indexation, resulting in the current maximum annual tax offset of $11,875 (i.e. 10% x $118,750).

48 The short point we wish to make in this regard is that when the transfer balance cap rules were introduced, the tax advantages available to persons in receipt of non-commutable defined benefit pensions were limited in a manner that took **careful account** of the existing tax treatment of those pensions. In stark contrast, the proposed Div 296 rules take **no account** of the fact that the existing tax rules applying to defined benefit pensions are **entirely different** from the tax rules applying to account-based pensions paid from private superannuation funds.

[5] Para 3.248 of the Explanatory Memorandum to *Superannuation (Objective) Bill 2016, Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016* and *Superannuation (Excess Transfer Balance Tax) Imposition Bill 2016.*

Summary

49 The real target of the proposed tax rules in Div 296 is the voluntary accumulation of funds of more than $3 million in an advantageous tax environment. The extension of the Div 296 rules in the manner proposed to cover a Statutory Pension Entitlement would result in an accruing tax liability on a notional accumulation of funds even though the person entitled to the pension has no control over the notional accumulation of funds and the actual pension, when paid, would be fully taxed subject only to a maximum annual tax offset of (currently) $11,875.

50 For persons (such as Commonwealth and Territory judges) in that position, the proposed Div 296 tax would not act as a limitation on existing tax benefits. It would bear no relation to the existing tax offset that applies to their pensions and, in many cases, would exceed the amount of the tax offset, possibly substantially, resulting in an imposition of Div 296 tax and income tax at a combined level that is greater than the income tax that would be imposed on a salary or on any other income derived by any other taxpayer.

51 This is not only discriminatory and inequitable, it is clearly contrary to the policy to which the proposed Div 296 tax is intended to give effect and consequently, it is unjustifiable from a tax policy perspective.

Retired judges would be particularly disadvantaged because pensions paid to retired judges would be taxed more heavily than any other form of income or profits

52 The impact of the proposed Div 296 tax would fall disproportionately and unfairly on retired Commonwealth and Territory judges, for three reasons.

53 First, during the judge's period of service, the judge will not have any ability to withdraw funds from a statutory superannuation account to pay Div 296 tax on the accruing notional "total superannuation balance" corresponding to the judge's entitlement to a statutory defined benefit pension.

54 Secondly, assuming that the judge's total Div 296 tax liabilities relating to his or her period of service are payable in the first year of retirement, the amount payable could represent a very substantial part of their pension in that year (as indicated in para 44 above) and, together with income tax on their pensions, could easily exceed

the amount of the pension.

55 Thirdly, in each subsequent year of retirement (as indicated in para 44 above), Div 296 tax payable by a retired judge in each subsequent year of retirement is likely to exceed the tax offset available in respect of the judge's pension, resulting in a total level of income tax that is higher than would be imposed on a salary earned by any employed person or on investment income or the profits of a business.

56 The benefit of a judicial pension is the assurance of a comfortable level of income to fund a dignified retirement that Parliament considers to be suited to a person who has occupied the position of a judge. That societal purpose will clearly be eroded if retired judges face ongoing income tax costs than are higher than those imposed on income or profits generally.

Div 296 tax is likely to be unconstitutional in its application to current and retired Commonwealth judges

57 There are clear indicators that the Bills and the accompanying Explanatory Memorandum recognise there is substantial doubt about the constitutional validity of the proposed Div 296 tax in its application to judicial pensions.

58 The Explanatory Memorandum specifically indicates (at 1.116 – 1.118) that, by reason of s 72(iii) of the Constitution, Div 296 tax will not be imposed on pension benefits of current Commonwealth judges while they continue in office. The Explanatory Memorandum makes the assertion (at 1.119) that "the constitutional restrictions do not apply to retired Commonwealth justices and judges". The fact that the Imposition Bill, unusually, contains a savings clause (proposed s 6) to sever and nullify the imposition of taxation, if that imposition would exceed the legislative power of Parliament, reveals substantial doubt about the accuracy of that proposition in its application to the proposed Div 296 tax.

59 As noted above, in *Austin & Anor v Commonwealth*, Gaudron, Gummow and Hayne JJ at [72] observed that a Commonwealth judge's "remuneration" which s 72(iii) of the Constitution requires not to be diminished during continuance in office, "includes non-contributory pension plan entitlements which are accruing under the federal judicial pensions statute": see also *Forge* at [76]. The entitlement to a pension in due course is part of a judge's *current* remuneration.

60 The AJOA has received advice from Nicholas Owens SC that, to the extent that it was considered necessary to insert the exemption in item 2 of the table in proposed ss 296-310 in order to avoid infringing s 72(iii) of the Constitution, the limited scope of the exemption would be ineffective to achieve its apparent aim in three respects.

61 First, the exemption in item 2 of the table in proposed ss 296-310 is not effective to avoid the imposition of the tax on a judge's entitlement to their judicial pension. That is because the value of a judge's entitlement to a pension under the *Judges' Pensions Act* (Cth) remains an integer in the calculation of Div 296 tax. In other words, even though that value is excluded from the definition of "superannuation earnings", it remains a component of the formula by which the percentage of those earnings that are "taxable superannuation earnings" is derived. The result is that a higher proportion of a judge's "superannuation earnings" will be taxable by reason of the judge's pension entitlements or, viewed another way, the judge will pay tax on the value of their pension entitlements.

62 Secondly, the limitation of the exemption in item 2 of the table in proposed ss 296-310 to judges who are currently serving is not effective to avoid the imposition of tax on a serving judge's entitlement to their judicial pension. That is because, for the reasons given in the preceding para, there is an immediate impact on a judge's tax liability.

63 Thirdly, the limitation of the exemption in item 2 of the table in proposed ss 296-310 to judges who are currently serving does not avoid the postulated issue under s 72(iii) of the Constitution because, for a judge who is still serving, the application of the tax following the judge's retirement represents an immediate reduction in the judge's present remuneration, of which future pension rights form a part.

64 Additionally, Mr Nicholas Owens SC has advised the AJOA that he considers that the limitation of the exemption in item 2 of the table in proposed ss 296-310 to judges who are currently serving does not avoid the postulated issue under s 72(iii) of the Constitution for a judge who has already retired, because s 72(iii) prohibits the reduction in remuneration rights (such as pension entitlements) that accrued while the judge held office, whether before or after the judge ceases to hold office.

65 The exemption in item 2 of the table in proposed ss 296-310 is thus ineffective to avoid the constitutional issue that presumably motivated its inclusion.

66 In our respectful submission, the proposed Div 296 tax is unconstitutional in its application to current and retired Commonwealth judges. It is likely that constitutional litigation would result if the Bills are passed. It would not be in the public interest for there to be litigation in the High Court (whose judges will be affected by Div 296 tax) between Commonwealth judges and the Commonwealth, particularly when insufficient consideration has so far been given to the important constitutional implications of the tax.

67 We respectfully suggest that, at least, the opinion of the Solicitor-General should be obtained in relation to all of the constitutional points that arise from the Bills, including whether the proposed legislation, in its application to Statutory Pension Entitlements of judges, is within the Commonwealth's taxing power and whether it amounts to an acquisition of property otherwise than on just terms contrary to s 51(xxxi) of the Constitution.

Particular adverse treatment of Territory judges and undermining of democracy and self- government in the Territories and the institutional integrity of the Territory Supreme Courts

68 The effect of Div 296 tax is harsh in its effect on Territory judges (both ACT and NT) because, unlike for State and Commonwealth judges, it will apply to judges who are currently serving.

69 In respect of Territory judges, the imposition of Div 296 tax would be particularly egregious. The accruing Statutory Pension Entitlements of Territory judges are already subject to tax under Div 293 and their pensions are subject to income tax. Div 296 tax would be the third form of tax imposed on their Statutory Pension Entitlements. In contrast, State and Commonwealth judges are not subject to Div 293 tax.

70 The Bills would override s 73(3A) of the *Australian Capital Territory (Self-Government) Act 1998* (Cth) and s 41(3) of the *Supreme Court Act* (NT) which make provision to the effect that the remuneration and allowances to which a judge

is entitled, shall not be diminished while the judge holds office.

71 As a matter of public interest, these Territory provisions should not so readily be overridden through a tax that will raise such small amounts of revenue. These provisions serve the important role, as already discussed, of protecting the independence and impartiality of Territory judges.

72 The application of Div 296 tax to Territory judges will interfere with democracy and self-government in the Territories and undermine the institutional integrity of the Territory Supreme Courts.

Conclusion

73 The proposed Div 296 tax would operate as a substantial tax in addition to normal income tax on defined benefit pensions which form part of the remuneration of judges, and would be contrary to the public interest because it would impinge upon the independence of the judiciary.

74 The differential application of the proposed Div 296 tax to State judges, Commonwealth judges (and different categories of Commonwealth judges, depending on the date of their appointment), and Territory judges will have adverse consequences for the judicial system. Div 296 tax would also create adverse consequences in terms of addressing the gender disparity in the composition of the Commonwealth and Territory courts.

75 The impact of the proposed Div 296 tax for Commonwealth and Territory judges would be entirely disproportionate to the strictly limited taxation concessions that apply to such pensions, and is likely to result in a much higher overall level of taxation that would be imposed on any other income derived by any other taxpayer. As a matter of tax policy and design and equity, this is unjustifiable.

76 Retired judges would be particularly disadvantaged because pensions paid to retired judges would be taxed more heavily than any other form of income or profits.

77 There is considerable doubt that the proposed application of Div 296 tax to judges' Statutory Pension Entitlements is constitutionally valid. It is undesirable to enact

taxation laws which are not certain in their operation.

78 Territory judges would be particularly disadvantaged by being immediately adversely affected by Div 296 tax. This will interfere with democracy and self-government in the Territories and undermine the institutional integrity of the Territory Supreme Courts.

79 The minor fiscal benefit to the Commonwealth cannot justify the erosion of Australia's system of democracy that Div 296 tax would create.

The Honourable Justice Michael Walton
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