REPORT

DEPARTMENT OF TREASURY AND FINANCE
ELECTRICITY INDUSTRY SUPERANNUATION SCHEME

June 2014

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Report

Parliamentary referral - *Ombudsman Act 1972*

Relevant government agencies	Department of Treasury and Finance Electricity Industry Superannuation Scheme
Ombudsman reference	2013/03747
Date of referral	25 September 2013
Issues	1. Whether any administrative error occurred in connection with the changes to the scheme rules made on 28 June 2002; and the preparation of an explanatory memorandum dated 27 June 2002 2. Whether the department misled the Crown Solicitor in seeking legal advice in 2007 3. Whether since 2002 the department or the EISS Board has provided misleading advice in connection with the Treasurer's decision on the method used by EISS to calculate its taxed-source pensions

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Preliminary matters

A. Jurisdiction

The parliamentary referral

On 25 September 2013, the Legislative Council of South Australia passed a resolution which, *inter alia*, referred a number of matters and their associated administrative acts to the Ombudsman pursuant to section 14 of the *Ombudsman Act 1972* for investigation (**the parliamentary referral**). The parliamentary referral followed representations made by the South Australian Government Superannuated Employees Association Inc. (**SA Superannuants**).

The parliamentary referral was in the following terms:

> That this council—
>
> 1. Notes the concern of pension scheme members regarding the Electricity Industry Superannuation Scheme (EISS) and the set of documents providing the basis of that concern provided to members of parliament by the organisation SA Superannuants and Mr Richard Vear, a pensioner of EISS;
>
> 2. Refers the following matters and their associated administrative acts to the Ombudsman, pursuant to section 14 of the *Ombudsman Act 1972*, for investigation and report on the EISS method for calculating its taxed-source pensions and compliance of that method with the *Electricity Corporations Act 1994* (as modified by the *Electricity Corporations (Restructuring and Disposal) Act 1999*) –
>   (a) probity of processes resulting in a letter dated 7 June 2002 addressed to the then under treasurer being received by the Department of Treasury and Finance and accepted as coming from the EISS board to advise that the board supported and recommended rule changes for EISS developed by the financial services firm Mercer;
>   (b) probity of processes resulting in receipt by the Department of Treasury and Finance of the Mercer explanatory memorandum dated 27 June 2002, which is a document that has been cited as providing evidence that the method for calculating EISS taxed-source pensions had no effect on employer costs;
>   (c) inconsistency between the claim made in the Mercer explanatory memorandum of 27 June 2002 that EISS rule changes would have no effect on employer costs and analyses contained in the Mercer reports of 1998 and 2004 showing that the rule now being used by EISS to calculate its taxed-source pensions would reduce employer costs if applied to pensions of the state pension scheme;
>   (d) probity of the decision to provide only the explanatory memorandum of 2002 and not the Mercer reports of 1998 and 2004 to the Crown Solicitor when advice was sought on compliance of the method with the Electricity Corporations Act 1994;
>   (e) probity of advice and recommendations of the Department of Treasury and Finance to the EISS board and the then treasurer, Kevin Foley, in connection with his authorisation of use of the method in June 2002 and to both Mr Foley and the Minister for Finance, Hon. Michael O'Brien MP, in connection with representations about the validity of the method that have been made by SA Superannuants and Mr Richard Vear;
>   (f) whether the method used to calculate EISS taxed-source pensions has reduced employer costs for those pensions compared to what the cost would be if the pensions had continued as untaxed-source pensions;
>   (g) whether the method complies with the Electricity Corporations Act 1994 including schedule 1, part F, clause 11: Treasurer may vary rules in relation to taxation, subclauses (1) and (2); and
>   (h) any other relevant matter.
>
> 3. Resolves that, in all the circumstances of the case, administrative acts associated with these matters warrant investigation by the Ombudsman despite the availability of any alternative appeal, reference, review or remedy of the passage of time since SA Superannuants and Mr Richard Vear had notice of the administrative acts.

Section 14(1) of the Ombudsman Act permits either House of Parliament, or a committee of Parliament, to refer to the Ombudsman for investigation 'any matter that is within the jurisdiction of the Ombudsman and which that House or committee considers should be investigated by the Ombudsman'.

I held concerns about my jurisdiction to investigate some of the matters contained in the parliamentary referral, in particular:

- whether the Electricity Industry Superannuation Scheme (**the EISS**) is an 'agency' to which the Ombudsman Act applies
- that the principal complaint was about the method for calculating EISS taxed-source pensions and therefore the relevant administrative act was a policy decision over which the Ombudsman has no jurisdiction (see *City of Salisbury v Biganovsky* (1990) 54 SASR 117)
- that the principal complaint about the method for calculating EISS taxed-source pensions relates to a decision that was made by the Treasurer, and the Ombudsman has no jurisdiction to investigate ministerial decisions
- whether the Ombudsman could satisfactorily complete an investigation of the matters concerning the Crown Solicitor because acts done by a person in the capacity of legal adviser to the Crown are excluded from the definition of 'administrative act' in section 3 of the Ombudsman Act.

Consequently I sought a legal opinion from Mr Stephen McDonald of Hanson Chambers.

Following receipt and consideration of Mr McDonald's advice, I determined that I would investigate certain of the matters referred to me by the Legislative Council, but not others.

First, Mr McDonald advised me that the better view is that the EISS Board is a body 'continued in existence for a public purpose by an Act' and is, therefore, an agency to which the Ombudsman Act applies. Mr McDonald also advised that it would seem that the individual members of the Board are agencies to which the Ombudsman Act applies. To the extent that the referred matters relate to administrative acts of the EISS, they are therefore within my jurisdiction.

Second, based on Mr McDonald's advice I determined to proceed as follows with respect to each of the substantive terms of the Legislative Council resolution:

(a) Probity of processes resulting in a letter dated 7 June 2002 addressed to the then-Under-Treasurer being received by the Department of Treasury and Finance and accepted as coming from the EISS Board to advise that the Board supported and recommended rule changes for EISS developed by the financial services firm Mercer;

I determined to investigate this matter, but only insofar as it relates to administrative acts by persons other than the Treasurer.

(b) Probity of processes resulting in receipt by the Department of Treasury and Finance of the Mercer Explanatory Memorandum dated 27 June 2002 which is a document that has been cited as providing evidence that the method for calculating EISS taxed-source pensions had no effect on employer costs;

I determined to investigate this matter, but only insofar as it relates to administrative acts by persons other than the Treasurer.

(c) Inconsistency between the claim made in the Mercer Explanatory Memorandum of 27 June 2002 that EISS rule changes would have no effect on employer costs, and analyses contained in the Mercer Reports of 1998 and 2004 showing that the rule now being used by EISS to calculate its taxed-source pensions would reduce employer costs if applied to pensions of the State Pension scheme;

The administrative acts associated with this paragraph are the preparation of the Mercer explanatory memorandum and the Mercer reports. These are the acts of Mercer LLC (**Mercer**), a global non-government company. In order to exercise jurisdiction in relation to these acts I need to be satisfied that they were done 'in the performance of functions conferred under a contract of services with the Crown or an agency to which [the Ombudsman] Act applies'.[1]

I am so satisfied, and I have considered this issue. However, for the reasons set out in this report I am not persuaded that the assumption which underlies this paragraph is correct. I do not consider that there is a reasonable basis for comparing the 2002 explanatory memorandum with the 1998 and 2004 reports, and accordingly I determined not to investigate this matter any further.

(d) Probity of the decision to provide only the Explanatory Memorandum of 2002, and not the Mercer Reports of 1998 and 2004, to the Crown Solicitor when advice was sought on compliance of the method with the Electricity Corporations Act 1994;

I determined to investigate this matter. However, I advised the parties that depending upon the particular factual circumstances, it may become apparent that the administrative acts to which this paragraph relates were acts done by a person acting in the capacity of legal adviser to the Crown, in which case it would then be apparent that I do not have jurisdiction to investigate it. If that occurs, I would desist from investigating it.

(e) Probity of advice and recommendations from the Department of Treasury and Finance to the EISS Board and the then Treasurer Kevin Foley in connection with his authorisation of use of the method in June 2002, and to both Mr Foley and the Minister for Finance, Hon Michael O'Brien MP, in connection with representations about the validity of the method that have since been made by S.A. Superannuants and Mr Richard Vear;[2]

I determined to investigate the process leading up to the Treasurer's decision, but only insofar as it relates to administrative acts by persons other than the Treasurer.

(f) Whether the method used to calculate EISS taxed-source pensions has reduced employer costs for those pensions compared to what the cost would be if the pensions had continued as untaxed-source pensions;

This matter is beyond my jurisdiction and I determined not to investigate it.

Mr McDonald advised me that the paragraph is framed in the abstract, as a pure question of law, and there is no administrative act associated with it. Further, even if the question posed in the paragraph could be connected with a particular act, it addresses the content of the ultimate decision, the decision of the Treasurer, which is not within the jurisdiction of the Ombudsman.

(g) Whether the method complies with the Electricity Corporations Act 1994 including Schedule 1, Part F, clause 11: Treasurer may vary rules in relation to taxation, sub-clauses (1) and (2); and

This matter is beyond my jurisdiction, for the same reasons as for paragraph (f), and I determined not to investigate it.

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[1] See paragraph (b) of the definition of 'administrative act' in section 3 of the Ombudsman Act.

[2] SA Superannuants is an organisation which represents the interests of some members of the South Australian State Pension Scheme. Mr Richard Vear is a member of the EISS who raised concerns about its operation, and who previously complained to this office about the matter. For ease of reading in this report I have used the term 'SA Superannuants" to include both the organisation and Mr Vear.

(h) any other relevant matter.

In course of my investigation I did not discover any other relevant matters which in my view required investigation.

In light of Mr McDonald's advice, I determined that I would investigate the four issues outlined above.

The Mercer 2002 memorandum

Paragraph (b) of the definition of 'administrative act' in section 3 of the Ombudsman Act specifies that such an act includes 'an act done in the performance of functions conferred under a contract for services with the Crown or an agency to which this Act applies'.

I have invoked this definition to consider the actions of Mercer, notably in relation to the preparation of the explanatory memorandum signed by Mr Allan Archer, Principal, and dated 27 June 2002 (**the 2002 memorandum**). It is my understanding that at the relevant times, Mercer were engaged to provide administration and actuarial advice to the EISS Board on the operation of the EISS.[3]

Allegation of apprehended bias

In response to my provisional report, SA Superannuants stated by letter dated 25 March 2014 that it held a reasonable apprehension of bias in the conduct of my investigation. In support of their contention, they referred to:

- the content of a paragraph in my provisional report, and an email which I sent to Dr Ray Hickman, a representative of SA Superannuants, on 18 March 2014 explaining the reasoning supporting that paragraph
- the fact that I described the department as having authorised the release of legal advice, rather than having relied on my legal powers to require the release
- a footnote outlining my interpretation of some legal advice
- my handling of evidence given by a former officer of the department, Mr Deane Prior
- the fact that the scope of my investigation largely reflects my previously suggested own initiative investigation
- the fact that whilst I stated that I have no power to investigate the advice given by Crown Law officers, I commented on the content of some legal advice
- the fact that they consider that I have not investigated the acts of persons who briefed legal advisers.

Because this allegation may raise a potential issue of maladministration in the office of the Ombudsman, I considered that I had an obligation to report it to the Office of Public Integrity (**OPI**). I did so on 31 March 2014, and provided my files in support of the report.

On 5 June 2014, the Independent Commissioner Against Corruption advised me that he did not consider that my conduct had 'enlivened any reporting obligations under the Directions and Guidelines'.

On 10 June 2014 he authorised me to publish the above statement in this report.

I therefore determined to finalise my investigation notwithstanding the allegation made by SA Superannuants.

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[3] Letter dated 4 December 2001 written by the Director, Superannuation (Policy) in the department to Mr Allan Archer of Mercer. See also the submission from the EISS Board, 2012 Ombudsman's inquiry into certain aspects of the Electricity Industry Superannuation Scheme (EISS), 15 November 2012 (**the EISS Board submission**) paragraph 26.

B. Standard of proof

The standard of proof I have applied in my investigation and report is on the balance of probabilities. However, in determining whether that standard has been met, in accordance with the High Court's decision in *Briginshaw v Briginshaw* (1938) 60 CLR 336, I have considered the nature of the assertions made and the consequences if they were to be upheld. That decision recognises that greater care is needed in considering the evidence in some cases.[4] It is best summed up in the decision as follows:

> The seriousness of an allegation made, the inherent unlikelihood of an occurrence of a given description, or the gravity of the consequences flowing from a particular finding, are considerations which must affect the answer to the question whether the issue has been proved … .[5]

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4 This decision was applied more recently in *Neat Holdings Pty Ltd v Karajan Holdings Pty Ltd* (1992) 110 ALR 449 at pp449-450, per Mason CJ, Brennan, Deane and Gaudron JJ.

5 *Briginshaw v Briginshaw* at pp361-362, per Dixon J.

Investigation

My investigation has involved:

- assessing the information provided by SA Superannuants in submissions dated 19 November 2012 (**the first SA Superannuants submission**) and 13 January 2014 (**the second SA Superannuants submission**).[6] I note that the first SA Superannuants submission was provided in relation to an earlier Parliamentary reference which lapsed, but in my view it contains relevant information for the purposes of this investigation. I note also that in response to a specific request from me, the second SA Superannuants submission included a separate document entitled *An argument against the proposition that Clause 11 does not preclude a reduction in employer costs*
- assessing the information provided by EISS in a submission dated 15 November 2012 (**the EISS Board submission**)
- considering a brief to counsel prepared on behalf of the EISS Board by DMAW Lawyers dated 1 November 2007; and the subsequent memorandum of advice from P A McNamara QC dated 7 December 2007
- considering clause 11 of Schedule 1 to the *Electricity Corporations Act 1994* (**clause 11**)
- considering clause 5 of the Electricity Industry Superannuation Scheme Trust Deed (**the Trust Deed**), set out in Schedule 1 to the Electricity Corporations Act[7]
- considering Rules 29-31 of the Rules of the Electricity Industry Superannuation Scheme operating in accordance with Schedule 1 of the Electricity Corporations Act and the Trust Deed established in accordance with that Act (**the scheme rules**)
- considering the Heads of Government Agreement on Superannuation (**HOGAS**)
- considering a departmental minute dated 26 June 2002 provided to the Treasurer to assist his decision-making on the 2002 changes to the scheme rules (**the departmental advice**)
- considering the 2002 memorandum
- considering legal advice provided to the department by the Crown Solicitor, dated 25 January 2006 and 26 November 2007
- considering legal opinions dated 29 August 2005 provided by DMAW Lawyers; and 7 December 2007 provided by P A McNamara QC
- interviewing Mr Prior. I did not consider it necessary to conduct this interview on oath
- interviewing Mr Jon Holbrook, EISS Board Chief Executive Officer, on oath[8]
- interviewing Mr Patrick McAvaney, Director, Policy and Governance, Super SA and Ms Alannah Pearce, Senior Policy Officer, Super SA on oath
- preparing a provisional report and sending it to the department; the EISS; Mr Prior; and SA Superannuants for comment
- considering the responses received
- reporting the matter to OPI and considering the response of the Independent Commissioner Against Corruption
- interviewing Dr Hickman and Mr Barry Foster (a member of SA Superannuants) on oath
- preparing this final report.

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[6] SA Superannuants provided an earlier version of this submission on 9 December 2013, but it did not include the relevant attachments.

[7] The Trust Deed is set out in Schedule 1 to the Act. Whilst Clause 13 of the Schedule and Clause 1 of the Trust Deed permits the separation of the Trust Deed from the Schedule, I understand that this has not occurred.

[8] At interview, which was conducted on 16 January 2014, Mr Holbrook was accompanied by Ms Suzanne Mackenzie from DMAW Lawyers, who acts for the EISS Board.

Responses to my provisional report

I published my provisional report to the department; the EISS; Mr Prior; and SA Superannuants on 4 February 2014.

On 28 February 2014, Mr McAvaney advised me that the department had no further comment to make.

By letter dated 28 February 2014, the EISS Board advised me that it had no issue with the conclusions reached, but there were some minor matters which required clarification or correction. I have noted these corrections as appropriate in this report.

By letter dated 26 February 2014 Mr Prior commented that:

- SA Superannuants is not recognised by the EISS Board as the representative body of their members including retired members, and is better described as a body that on this matter purports to represent the interests of some members of the EISS scheme
- he attended several of the EISS Board meetings held in 2002 to consider the matter. It was his impression that the Board had difficulty understanding the actuarial explanations provided; that the Board recognised that the Treasurer would accept the advice of the actuarial adviser; and that consequently the Board agreed it should endorse the proposed formula adjustment
- a copy of the Mercer worksheets were provided as background material that went to the Treasurer to assist his decision-making in June 2002. Mr Prior noted that he had retained a copy of the worksheets, and had shown them to me at his interview with me.

By letter dated 26 February 2014 SA Superannuants commented on my provisional report, and made 14 requests of me. The matters it raised were:

- this investigation is essentially the own initiative investigation which I proposed in 2012 and which it rejected
- it maintains that I have not followed my own advice not to construe clause 11 to advance a position which a proponent may hold
- it is confident that I am wrong in my views that:
    - clause 11 does not preclude a reduction in employer costs
    - HOGAS has as one of its intentions, a reduction in employer costs for public sector superannuation schemes
    - a superannuation fund trustee is under no obligation to defend the interests of its beneficiaries in the circumstances applying to the rule changes made by the Treasurer in June 2002
    - there are differences between the State Pension Scheme and EISS that make the 1998 Mercer Report not relevant to EISS
- it seeks further detail on why some elements of the reference are outside my jurisdiction. It believes I should have exercised my power under section 28 of the Ombudsman Act to approach the Supreme Court for a ruling on my jurisdiction, and it considers that there is a lack of procedural fairness in my failure to provide reasons for matters being outside my jurisdiction. I have provided further explanations in this report
- it seeks clarification of my comments regarding the scope of Mr Clive Brooks' application to the department under the *Freedom of Information Act 1991*
- it seeks:
    - a copy of the letter dated 4 December 2001 written by the Director, Superannuation (Policy) in the department to Mr Allan Archer (**the 4 December 2001 letter**). I provided representatives of SA Superannuants with a copy of this letter on 17 June 2014
    - a statement in my final report that the 4 December 2001 letter should have been provided in response to Mr Brooks' FOI application
    - an explanation of why it was not so provided

  - a statement in my final report outlining what else was in the 4 December 2001 letter
  - clarification of whether there was any response by the department to the 4 December 2001 letter
  - that I should establish whether the department has documentation of the remuneration received by Mr Archer for the service described in the 4 December 2001 letter
  - confirmation that an invoice dated 10 September 2002 referred to the work done in response to the 4 December 2001 letter, and an explanation of why the department paid this invoice when it was addressed to the EISS Board
- clarification of the amount of the tax savings to the EISS Board of the pre-July 1988 Funding Credits; and a reconciliation of advice given to my investigation with the EISS Board's 2005 Annual Report
- clarification of its response to my suggestion that it should ask the Crown Solicitor whether he considers that he was misled by the department when it provided instructions for the purposes of seeking legal advice. It considers that the Crown Solicitor's response addressed a different piece of advice, and foreshadowed its intention to again raise the matter with the Crown Solicitor
- it requested that I should interview Dr Hickman, Mr Brooks and Mr Foster on oath.

I subsequently sought clarification from the department as to why the 4 December 2001 letter was not discovered when the FOI application was made by Mr Brooks. On 27 June 2014, the department advised me as follows:

> … we are not able to provide a definitive explanation as to why the document was not produced as part of the FOI application made on 15 February 2012. However, an examination of the history of the matter reveals that the search appeared to be conducted under the assumption that the relevant document was held by the "Electricity Reform and Sales Unit" (which I understand to have been established as a division of DTF).[9]

In my view this is not an unreasonable response.

I also sought clarification from the EISS Board about the amount of tax savings arising from the pre-July 1988 Funding Credits. I have included its response in this report.

On 10 March 2014, I wrote to Dr Hickman, Mr Brooks and Mr Foster proposing an opportunity for them to be interviewed about their submissions. However, on 17 March 2014, Dr Hickman on behalf of SA Superannuants sent an email to me alleging apprehended bias in my investigation. I have noted above that on 25 March 2014 SA Superannuants wrote to me detailing its reasons in support of this allegation.

After I dealt with that allegation in the manner outlined above, I again invited Dr Hickman, and Mr Foster to be interviewed. I interviewed them on oath on 17 June 2014. At that interview I outlined my response to SA Superannuants' requests. In particular, I advised them that I did not intend to further investigate the circumstances of the 2001 contract between the department and Mercers, as evidenced by the letter dated 4 December 2001.

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[9] Email from a departmental officer, 27 June 2014. Mr Brooks' application under the FOI Act sought access to the following:
(a) The documents by which the Department of Treasury and Finance commissioned the document entitled: "Explanatory Memorandum," prepared by MERCER Human Resources Consulting, dated 27 June 2002, and signed by Allan Archer, Principal,
(b) The invoice relating to the aforesaid Explanatory Memorandum provided to the Department of Treasury and Finance.
It appears to me that the 4 December 2001 letter was caught by this application, and should have been disclosed in response to it. I have commented on sufficiency of search issues in my recent report 'An audit state government departments' implementation of the *Freedom of Information Act 1991(SA)*', and made a series of recommendations designed to improve agencies' performance in this regard: see http://www.ombudsman.sa.gov.au/wp-content/uploads/An-audit-of-state-goverment-departments-implementation-of-the-Freedom-of-Information-Act-1991-SA.pdf, recommendations 13-16.

I have considered the above comments made by the parties, and where I consider it appropriate I have amended this report in response.

Background

1. The EISS is a superannuation scheme governed by Schedule 1 of the Electricity Corporations Act, for the benefit of former employees of the Electricity Trust of South Australia (**ETSA**). Members of the EISS are classified by the section of the scheme rules (known as 'Divisions') in which their benefits are specified. This investigation relates to the pension scheme, which is covered by Division 3 of the scheme rules.

2. The EISS Board has described the operation of the scheme as follows:

    17. The Scheme's history is generally split into pre-privatisation and post privatisation (of the Electricity Trust of South Australia, or ETSA).

    18. Before privatisation of ETSA (in 2000) the Scheme was an unfunded, constitutionally protected, exempt public sector scheme. Most members were provided with defined benefits, and ETSA only paid contributions in to the Scheme when a benefit was payable (i.e. the money came in, and then went straight out again). Members contributed from their salaries, and this money was invested by the EISS Board. The EISS was not a taxpaying fund, which meant that members paid a higher rate of tax on their benefits than members of tax-paying superannuation funds.

    19. After privatisation, the Scheme became a funded, taxed industry fund, but continued as an exempt public sector scheme. There was an unfunded liability, which the new employers (being the private sector companies that acquired the privatised assets of ETSA) were required to pay off over five years (this was completed in 2005). Employer contributions and investment earnings became taxed (in accordance with most funds) and the tax on benefits was reduced (and is now in line with most funds).

    20. The tax offset rules were introduced at this point. In light of the tax changes outlined above, if there were no corresponding adjustment to members' gross benefits, the employers would be required to cover the tax payable from the fund and members would receive the same benefits – with the application of a lower tax rate (this has generally been referred to as a potential for a "windfall gain" for members).

    21. As an exempt public sector scheme, the Scheme remains exempt from the Commonwealth prudential regulatory framework, known as the Superannuation Industry (Supervision) legislation (or 'SIS'), which applies to most private sector funds. However, the EISS Board complies with SIS as far as practicable.[10]

3. The EISS still attracts new members into its Accumulation Division, but two of the defined benefit divisions (including the pension scheme) were closed to new entrants in or around 1988. SA Superannuants represent some of the beneficiaries of the scheme, both existing pension-holders and current employees who expect to receive pensions from the scheme in due course. There are about 400 pension beneficiaries under Division 3 of the scheme, approximately 160 of whom are still in employment. Most of those are in their 50s with the youngest being 42 years of age.[11] The retired scheme members are mostly in their 60s.

Constitutional protection[12]

4. Before 1 July 1988 superannuation funds paid no tax on the money received as contributions or on the earnings of assets they held. On 1 July 1988 a 15% contributions tax was introduced on contributions made from pre-tax income of members and/or employers and a tax rate of up to 15% became payable on the earnings of assets.

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[10] EISS Board submission, paragraphs 17-21.
[11] He was 17 years of age when the scheme was closed off in 1988.
[12] This section draws heavily on the first submission from SA Superannuants.

5. However, constitutional limitations on the taxation power of the Commonwealth allowed state governments to continue running superannuation funds that were not subject to the new taxation regime applying from 1 July 1988. By the mid-1990s all state governments other than South Australia and Western Australia had opted to allow many of their funds to become subject to the new regime.[13] SA Superannuants attributes the reason for these decisions as being because they provided substantial net benefits to most members of the pension schemes without significant additional cost to government employers.

6. The government funds which were not subject to the taxation arrangements introduced on 1 July 1988 are called constitutionally protected and/or untaxed funds. Pensions paid from those funds are referred to as untaxed-source pensions. Where funds are subject to the taxation arrangements introduced on 1 July 1988 they are called taxed funds, and the pensions are called taxed-source pensions.

7. The effect of the taxes on fund income introduced on 1 July 1988 was to reduce the assets of each taxed fund, compared to what those assets would have been if it had continued as an untaxed fund. Consequently, the same level of employer contributions paid into a taxed fund on the one hand and an untaxed fund on the other hand, would have produced smaller pensions paid from a taxed fund.

8. In order to overcome this effect, the Commonwealth government reduced personal income tax on the resulting pensions. This was achieved by permitting a 15% tax offset claimable by recipients aged 55 and over, calculated on the entire taxable amount of the pension. By contrast, only the fraction of the pension accruing after 1 July 1988, and funded by employers, was reduced by 15% due to the new taxation arrangements. This situation gave rise to the Pre July 1988 Funding Credit (**PJFC**) discussed below.

9. By regulation made by the Commonwealth on 29 May 2002, the EISS lost its constitutional protection with effect from 1 July 2000. The EISS therefore became a taxed complying superannuation fund from that date.[14]

Variation of the EISS Rules

10. This investigation arises from a decision made by the Treasurer on 28 June 2002 to vary the rules of the EISS. The variation was achieved by the making of new rules purporting to be in accordance with clause 11. They took retrospective effect from 1 July 2000, when the EISS lost its constitutional protection.

11. Whilst the EISS remained constitutionally protected (i.e. for the period prior to 1 July 2000) the contributions to the EISS and income earned on assets in the scheme were not subject to taxation. Accordingly:
    - employer contributions and investment income were not taxable, as compared to a taxed fund where employer contributions and investment income are taxed at 15%
    - taxable lump sum benefits were taxed when paid to members at a higher rate (i.e. 30%) than for benefits paid from a taxed scheme (i.e. 15%)
    - the taxable portion of pension benefits were not entitled to a 15% rebate which was available to pension benefits paid from a taxed scheme.[15]

12. The EISS Board has commented to my investigation on the implications of the change to the constitutional status of the EISS as follows:

    > 36. If the rules of the Scheme had not been varied in response to the Scheme becoming a taxed Scheme after privatisation there would have been significant cost implications for

[13] However, Schedule 4 of the *Income Tax Assessment Regulations 1997* shows constitutionally protected funds in all States.
[14] Explanatory memorandum, p1.
[15] EISS Board submission, paragraph 35.

employers participating in the Scheme and significant net or after tax benefit improvements for members.

37. As a defined benefit scheme, the employers bear the risk of funding the benefits. Accordingly, when employer contributions commenced to be taxed in the Scheme from 1 July 2000, the cost of funding the gross benefits payable to members also increased – so without rule amendments to reduce members' gross benefits employers would have borne the cost of taxation payable by the Scheme. The EC Act allowed the Treasurer to introduce rules to minimise the extra cost to employers.

38. Also, without rule amendments to reduce members' gross benefits, members would have generally received a significant benefit improvement after tax – i.e. they would have been entitled to the same gross benefit from the Scheme, but would have been treated more favourably in relation to the tax payable on their benefits:
    - the lower tax rate of 15% would have applied in the case of lump sums; and
    - the 15% rebate would have been available in the case of pensions.[16]

13. SA Superannuants does not dispute that the Treasurer's decision to vary the EISS rules complied with one essential obligation under clause 11, namely that after tax benefits for existing members were not lower than would have applied if the scheme remained untaxed. However, SA Superannuants asserts that the decision did not comply with another obligation imposed by clause 11, namely that the costs to employers should not reduce as a result of a variation of the rules. For the reasons explained below, I do not agree that such an obligation in fact existed.

14. The consequence of the position put by SA Superannuants is that the existing members missed out on the 'windfall' gain that could have accrued to them, because employer costs were in fact decreased. In this respect, SA Superannuants contends that the members of EISS were treated less favourably than comparable schemes in other jurisdictions, and less favourably than should be the case for members of the state pension scheme if a similar adjustment is made to that scheme.

15. I understand that SA Superannuants is concerned about the precedent that has apparently been established. It fears that, should the government decide to move the broader state pension scheme into a taxed environment, it may seek to use a similar process to that adopted in the case of the EISS to reduce the gross benefits of pensions paid to retired public servants.

16. However, it is a question of policy - and hence outside my jurisdiction - as to whether in the case of EISS it was preferable for the 'windfall' gain to accrue to the existing members, or to the employers to reduce the cost of the scheme.

17. For the reasons explained above under the heading 'Jurisdiction', this investigation has been limited to a consideration of various administrative acts surrounding the Treasurer's decision to vary the scheme rules.

[16] EISS Board submission, paragraphs 36-38.

Relevant law/policies

18. The EISS Scheme is governed by Schedule 1 of the Electricity Corporations Act. It is administered by the EISS Board in accordance with the provisions of the Trust Deed[17] and the scheme rules.

19. Clause 5 of the Trust Deed provides as follows:

5—Reduction in benefits on changes in taxation

(1) Subject to subclause (3), where the cost to employers of maintaining the existing level of benefits is increased by a change in the incidence of taxation occurring after the Scheme loses its status as a constitutionally protected fund under the *Income Tax Assessment Act 1936* of the Commonwealth, the level of benefits is reduced to the extent necessary to avoid an increase in that cost.

(2) The extent of the reduction in the level of benefits under subclause (1) must be determined by the Trustee on the advice of an actuary.

(3) If the Trustee and all the employers agree that subclause (1) will operate to reduce the level of benefits to a lesser extent than is provided by that subclause, the subclause will operate in accordance with the agreement.

20. Clause 11 of Schedule 1 to the Electricity Corporations Act provides:

11—Treasurer may vary Rules in relation to taxation

(1) The Treasurer may, after consultation with the trustee of the Scheme, insert into the Rules a rule or rules relating to changes in benefits for members and employer costs in relation to those benefits, following the Scheme's loss of constitutional protection.

(2) A rule inserted by the Treasurer may—
(a) prescribe a decrease in the level of gross benefits; or
(b) require benefits to be paid on an untaxed basis or partly on an untaxed basis; or
(c) make provisions of the kind referred to in both paragraphs (a) and (b),
in order to avoid or reduce an increase in employer costs caused by changes in the incidence of taxation as a result of the Scheme's loss of constitutional protection.

(3) Subject to subclause (4), the change in benefits effected by a rule made under this clause must not result in the level of net benefits to which a member, or a person in respect of a member, is entitled being less than the level of net benefits to which he or she would have been entitled if the Scheme had not lost constitutional protection.

(4) The level of net benefits to which a member, or a person in respect of a member, is entitled may be reduced below the level permitted by subclause (3) to avoid or reduce an increase in employer costs attributable to tax under the *Superannuation Contributions Tax (Assessment and Collection) Act 1997* of the Commonwealth in relation to the member.

(5) A rule made under this clause may operate differently in relation to—
(a) different classes of members;
(b) different classes of benefits;
(c) different classes of components of benefits.

(6) A rule made under this clause—
(a) must be made by notice in writing given to the trustee of the Scheme before the relevant day;
(b) may be varied or revoked by the Treasurer by notice in writing to the trustee before that day;

[17] The Trust Deed is set out in Schedule 1 to the Act. Whilst Clause 13 of the Schedule and Clause 1 of the Trust Deed permits the separation of the Trust Deed from the Schedule, I understand that this has not occurred.

(c) is not subject to the *Subordinate Legislation Act 1978*.

(7) The trustee of the Scheme may vary or replace a rule inserted in the Rules under this clause in the same manner as it can vary or replace any of the other rules of the Scheme.

(8) In this clause—
level of gross benefits in relation to a member means the amount of the benefits to which the member, or another person in respect of the member, is entitled under the Scheme before tax attributable to those benefits has been paid or allowed for;

level of net benefits in relation to a member means the amount of the benefits to which the member, or another person in respect of the member, is entitled after tax attributable to those benefits has been paid or allowed for using the tax rates applicable on the day on which the Scheme loses constitutional protection and based on the assumption that the member has reached the age of 55 years;

the relevant day means the day on which the approval of the Treasurer ceases to be required for the variation or replacement of the Rules.

(9) For the purposes of this clause—
(a) benefits are paid on an untaxed basis where the trustee of the Scheme has made an election under the *Income Tax Assessment Act 1936* of the Commonwealth as a result of which the person receiving the benefits is liable for a higher rate of tax in relation to them;
(b) the Scheme loses constitutional protection when it ceases to be a constitutionally protected fund for the purposes of the *Income Tax Assessment Act 1936* of the Commonwealth.

21. Rule 29 of Division 1 of the scheme rules provides as follows:

Taxation Reduction of Benefits

29.(1) This Rule does not apply to a benefit or part thereof payable under the Rules that is either -
(a) a lump sum paid where the taxable component of the superannuation benefit consists wholly of an element untaxed in the fund;[18] or
(b) a pension paid where the taxable component of the superannuation income stream consists wholly of an element untaxed in the fund;[19] or
(c) a benefit derived from Additional Voluntary Contributions, or
(d) a benefit payable under Division 5 of these Rules after 1 July 2002.

(2) Notwithstanding any other provision of the Rules, each benefit or part thereof payable under the Rules (other than a benefit or part thereof listed in sub-rule (1) of this Rule) will be reduced in accordance with a formula determined by the Superannuation Board on the advice of the Actuary.

(3) In the case of a benefit or part thereof paid as a lump sum, the formula determined in accordance with sub-rule (2) of this Rule shall be such as to ensure that:

(a) the amount of the reduced benefit or part thereof which would be received after tax, assuming that taxation at the tax rates set out in column B of Schedule 1A of Division I of these Rules is applied to the reduced benefit or part thereof
equals

(b) the amount of the benefit or part thereof prior to its reduction by the formula which would be received after tax, assuming that taxation at the tax rates set out in column C of Schedule 1A is applied to the benefit or part thereof prior to its reduction by the formulae,

[18] This paragraph was replaced in June 2007.
[19] This paragraph was replaced in June 2007.

PROVIDED THAT in the case of a Member who was employed by a Consenting Employer immediately prior to becoming entitled to the payment of a lump sum benefit, if such formula causes the reduction in that part of the taxed element of the post June 83 component (which did not arise from a taxed rollover into the Scheme) to exceed 15% of that part, the reduction on that part must be 15%. In the application of this proviso it must be assumed that the taxation laws that applied on 1 July 2000 continue to apply.[20]

In determining whether the formula determined in accordance with sub rule (2) of this Rule satisfies the condition set out under this sub rule (3) it must be assumed in respect of each of paragraphs (a) and (b) of this sub rule (3) that the lump sum is taxed using the tax rates set out under Schedule IA as if the provisions relating to the taxation of superannuation lump sums (including from a taxed source and from an untaxed source, as applicable) under the taxation laws that applied before 1 July 2007 continued to apply.[21]

(4) In the case of a benefit paid as a pension, the formula determined in June 2007 in accordance with sub-rule (2) of this Rule shall be such as to ensure that:

(a) the amount of the reduced pension from a taxed source which would be received after tax and after taking into account a taxation rebate on pension payments at the rate of 15%;[22]

equals

(b) the amount of the pension prior to its reduction which would be received after tax assuming that it is paid as a pension from an untaxed source.[23]

(5) The formula for calculating the amounts received after tax, in accordance with paragraphs (a) and (b) of sub rule (4) of this Rule, shall:

(a) take into account the personal income tax scale applicable at the time the pension commences and shall assumed that the pensioner receives no taxable income other than the pension;

(b) in respect of the period from 1 July 2007, assume the pension is taxed as if the provisions relating to the taxation of pensions (including from a taxed source and from an untaxed source, as applicable) under the taxation laws that applied before 1 July 2007 continued to apply.[24]

(6) Where a member contribution in respect of any period after 1 July 2002 (other than an Additional Voluntary Contribution) has been paid by a Member and has not been paid by an employer in accordance with Rule 8A, the reduced benefit determined in accordance with sub-rule (2) of this Rule shall be increased by an amount calculated in accordance with a formula determined by the Superannuation Board on the advice of the Actuary to reflect the excess (if any) of-

(a) 15% of such member contributions after 1 July 2002, accumulated with interest at the Declared Rate,

over

(b) 15% of those member contributions without interest.

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[20] This paragraph was inserted 29 August 2008.
[21] This paragraph was inserted in June 2007.
[22] This paragraph was amended in June 2007.
[23] This paragraph was amended in June 2007.
[24] This subrule was substituted in June 2007.

Whether any administrative error occurred in connection with the changes to the scheme rules made on 28 June 2002; and the preparation of an explanatory memorandum dated 27 June 2002

22. SA Superannuants asserts in essence that in providing advice to the Treasurer about the making of the rules, the department and/or the EISS Board did not properly explain that the 'windfall' gain occasioned by the change to the scheme's tax status would accrue to employers to reduce the cost of the scheme; rather than being paid to members of the scheme through a favourable adjustment to the calculation of their revised benefits.

23. I have considered seven questions relevant to this issue. In formulating these questions I have endeavoured to summarise the various assertions of administrative deficiency made by SA Superannuants.

Was there any requirement that employer costs should not be reduced?

24. A threshold question is whether the relevant provisions in the EISS framework, including clause 11 and the scheme rules, required that employer costs should not be reduced. In my view, many of the submissions made by SA Superannuants assume that clause 11 prevents the making of rules which have the effect of reducing employer costs.

25. However, having considered the terms of clause 11 and the rules, I see no grounds to support an assertion that any variation of the rules should not have reduced employer costs. I appreciate that SA Superannuants has put the view firmly to me that clause 11(2) does operate to preclude a reduction in employer costs. I do not agree.

26. In my view, clause 11(2) simply permitted the Treasurer to make rules which decreased member benefits, so as to avoid an increase in employer costs resulting from changes in the incidence of taxation following from the EISS's loss of constitutional protection. Its introductory words specify that the Treasurer 'may' make such a rule. I imagine that the framers of the clause considered it to be necessary because it is unusual for member benefits in a superannuation scheme to be reduced. But clause 11(2) did not prevent a 'windfall' gain being used to reduce employer costs: indeed, it says nothing about such an occurrence.

27. I am conscious that my views about this issue have a significant impact on the contentions advanced by SA Superannuants. As a result, I provided it with an opportunity to address this issue specifically, which it did by letter dated 8 January 2014; and in its second submission. I set out below my views on the matters which SA Superannuants raised.

Prior consistent statements

28. First, SA Superannuants states that I am the first person to say to it that the rule for reducing pensions can be valid even if it reduces employer costs.[25] I do not agree that this is so. The Acting Treasurer advised SA Superannuants in a letter dated 12 October 2006 as follows:

> In your letter you state that the legislation covering the EISS provides that any rule inserted following the move of the fund into the taxed environment may reduce gross benefits "but only to the extent needed to avoid or reduce an increase in employer costs arising from a change in

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[25] SA Superannuants, *An argument against the proposition does not preclude a reduction in employer costs*, 14 January 2014, p1.

the incidence of taxation". The quote used in your letter is not a correct reflection of the provisions of the Act.[26]

29. I consider that this is an early indication to SA Superannuants that its interpretation of the effect of clause 11 is misconceived. In my view it is consistent with the conclusion which I have reached, namely that the legislative scheme does not prevent the reduction of employer costs in circumstances such as those which occurred. However, since that time SA Superannuants has continued to maintain that clause 11 should be interpreted in the way it proposes. In response to my provisional report it advised me that it considers that it is significant that the Acting Treasurer's letter quoted in the preceding paragraph was written before formal legal advice was obtained from Mr Stephen McDonald of the Office of the Crown Solicitor.[27]

Other possible wordings of clause 11

30. Second, SA Superannuants suggests that if it had been the intention of clause 11 to permit the possibility that employer costs may reduce, it would have been worded differently. It provides several possible alternatives to the existing wording of clause 11 seeking to demonstrate this contention.

31. With respect to the position advanced SA Superannuants, I consider that approach to be speculative. In my view the words of clause 11 must be interpreted according to their plain meaning, not construed to advance a position which a proponent may hold.

Other legal opinions

32. I advised SA Superannuants that I consider that my view is consistent with other legal opinions provided on related topics. SA Superannuants stated in response that those other opinions have not directly addressed the topic, and so cannot be considered relevant.[28]

33. It is true that the legal opinions have not directly addressed the topic of whether clause 11 operated to prevent the making of a rule which permits a 'windfall' gain being used to reduce employer costs. However, I consider that the opinions can provide some illumination on the question of whether clause 11 operated in that way; and in my view there is nothing in those opinions which renders that construction wrong. I set out below a summary of these opinions.

34. First, there is advice provided by Mr Chad Jacobi of the Crown Solicitor's Office on 25 January 2006. The department has provided me with a copy of that advice, and authorised me to disclose its substance. The advice notes that some EISS members had argued that clause 11 provides a guarantee that the level of net benefits to which a member is entitled will not be less than the net benefits to which he or she would have been entitled if the EISS had not lost constitutional protection; and that the state had an obligation in effect to 'make up the difference'. The advice concludes that the state has no such obligation.

35. Second, there is advice provided by Mr Stephen McDonald of the Crown Solicitor's Office on 28 November 2007.[29] The department has provided me with a copy of that

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[26] Letter from Hon Paul Holloway MLC, Acting Deputy Premier and Acting Treasurer to Mr Vic Potticary, SA Superannuants, 12 October 2006.

[27] The nature of this advice is outlined in paragraph 35. I note that the Acting Treasurer's letter post-dates the advice provided by Mr Chad Jacobi (outlined in paragraph 34).

[28] SA Superannuants, *An argument against the proposition does not preclude a reduction in employer costs*, 14 January 2014, pp 3-5.

[29] Mr McDonald's previous involvement in the matter was not known to me when I sought his advice on the Ombudsman jurisdictional questions arising under the Parliamentary referral. This is a different legal question from that upon which he provided advice to the department in 2007. He has also advised me that until it was brought to his attention on 3 February 2014, he had not remembered and was not aware that he had provided the advice to the department.

advice also, and has authorised me to disclose its substance. The advice includes the following statement:

> The purpose of the power granted to the Treasurer by clause 11 was to enable the reduction or complete avoidance of an increase in employer costs (ie, an increase in employer contributions to the fund) which would have otherwise resulted from the shortfall created by the imposition of a significant tax liability on the fund. The power in clause 11 did not extend to the making of a rule that provided for a total reduction in gross benefits which was greater than that which is required to avoid an increase in employer costs. Put another way, the power in clause 11 could not be used to insert a rule which had the effect of decreasing employer costs.[30]

36. Mr McDonald's advice concludes that 'on the assumption that the actuarial calculations can be justified, so that it could be demonstrated, if necessary, that the level of reduction in gross benefits effected by the insertion of Part XV into the Rules did have the effect of reducing or avoiding an increase in employer contributions and did not go beyond what was necessary to achieve that purpose … the insertion into the Rules of Part XV by the Treasurer is not invalid'. In support of this conclusion, he noted that:

> The extent of the reduction in gross benefits resulting from the insertion of the new rules has been justified actuarily in the Explanatory Memorandum which has been provided to me. I am not in a position to provide advice as to the accuracy of the actuarial calculations underlying the assertions in that Explanatory Memorandum. However, assuming that the assertions are correct, it appears that, had the Treasurer determined to insert a rule providing for a lesser reduction in gross benefits, that rule would have resulted in a shortfall in the fund such that, in order for the benefits to be paid to members, it would have become necessary to increase employer contributions to the fund. It follows that the rules which the Treasurer did insert were rules which had the effect of reducing or avoiding an increase in employer costs, as required by clause 11.

37. Mr McDonald's advice also explains the effect of the 25 January 2006 advice provided earlier by Mr Jacobi as follows:

> Mr Jacobi's advice did not directly state that the variations to the Rules made on 28 June 2002 were legal. Mr Jacobi advised more generally that, where factors other than a change to the Rules (factors such as reductions in Commonwealth Income Tax or expansions of Income Tax brackets) produce the result that members of the EISS are entitled to lower net benefits, clause 11 of Schedule 1 does not require the Treasurer or the State to compensate those members for any reduction in benefits. Clause 11(3) does not operate as a general guarantee that the net level of benefits to which a member is entitled cannot fall below that to which the member would have been entitled had the Scheme not lost constitutional protection: it merely restricts the effect of rules made under clause 11(1) so that those rules could not themselves have that effect.

38. Third, I consider that my conclusion is consistent with advice provided to the EISS Board by DMAW Lawyers in 2005.[31] This advice was provided in response to a question concerning which marginal tax rate of a pensioner the EISS Board should apply in calculating a benefit reduction. The advice relevantly concluded that whilst a net pension benefit 'may in some cases be less than is required by the calculation under clause 11 [this] will not invalidate rule 29 in its entirety, but will only cause it to be construed in those cases so that the higher net benefit applies'.

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[30] I acknowledge that the last sentence in this extract on its face provides support for the construction which SA Superannuants would urge, namely that the power in clause 11 could not be used to insert a rule which had the effect of decreasing employer costs. However, I consider that this statement is not consistent with the general tenor of the preceding sentences in this extract, and of the advice in total. In any event this is a different question to whether the clause prevented the making of a rule which had the effect of applying a windfall gain to reduce employer costs.

[31] Letter of advice dated 29 August 2005 (Attachment 9 to the brief to counsel dated 1 November 2007).

39. Fourth, my conclusion is also consistent with advice provided to the EISS Board by P A McNamara QC in 2007.[32] In this case, the principal question upon which advice was sought was whether rule 29(3) is invalid because it does not satisfy the 'no worse off' test for the Treasurer's power to vary the rules under clause 11(3).

40. The McNamara advice confirmed that clause 11(2) is a spent force; does not bind the Board; and is not now relevant to the correct interpretation of sub-rule 29(4).[33] The advice also concluded that 'sub-clause 11(3) does not bind the Board, and cannot be taken into account in construing sub-rule 29(3)'. [34] This position applies because:

> Clause 11 required that particular rules be inserted having a particular effect on the day on which the Scheme lost its constitutional protection. That day has come and gone. At the same time, the Treasurer's powers under Clause 11 have expired.[35]

Alleged subsequent departmental acknowledgement

41. SA Superannuants contends that the department has since acknowledged that the variation of the scheme rules 'were forbidden … to have the effect of reducing employer costs'.[36] They quote in support the following comment from the Minister for Finance:

> The formula that reduced gross pensions was determined actuarially in order to comply with the provisions of Clause 11(2) Part F of Schedule 1 Superannuation of the *Electricity Corporations Act 1994.* It was determined in a manner to avoid or reduce an increase in employer costs, but not reduce existing employer costs. It also satisfied the Act by ensuring that members received a net benefit that was not less than their existing net benefit applying before the fund moved into the taxed environment.[37]

42. I do not agree that this statement supports the acknowledgement which SA Superannuants contends has been made, that the rules 'were forbidden' from reducing employer costs. The statement simply outlines the fact that the intention of the rules was not to reduce employer costs, and in my view is consistent with the explanation of the purpose of the variation of the scheme rules as contained in the 2002 memorandum.

43. In any event, whether the department has previously made an acknowledgement is not determinative of the proper construction of clause 11.

The Heads of Government Agreement on Superannuation

44. SA Superannuants asserts that HOGAS 'placed an obligation on the State Government to ensure that tax outcomes for EISS members were the same as occurred in the other Australian jurisdictions'.[38] It quotes the following Paragraph from HOGAS:

> The Commonwealth and the State and Territory Governments recognise the need to apply national standards to certain aspects of superannuation without distinguishing between employees of the public and private sector. For example, it is important that members' accrued benefits are securely protected, and there is consistency of taxation outcomes for members' superannuation benefits.

45. In my view, the quoted extract does not support a suggestion that there should be equity as amongst members of public sector schemes in Australia. It states that

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[32] Advice provided to the EISS Board by P A McNamara QC, 7 December 2007, paragraph 234.
[33] Advice provided to the EISS Board by P A McNamara QC, 7 December 2007, paragraph 228.4-228.5.
[34] Advice provided to the EISS Board by P A McNamara QC, 7 December 2007, paragraph 238.
[35] Advice provided to the EISS Board by P A McNamara QC, 7 December 2007, paragraph 46.
[36] Second SA Superannuants submission, p25.
[37] Second SA Superannuants submission, p24. I understand that the quoted extract is a response given by the Minister for Finance to a question asked by Hon Iain Evans MP in a letter to the Minister dated 25 May 2012.
[38] SA Superannuants, *An argument against the proposition does not preclude a reduction in employer costs*, 14 January 2014, pp 5-6.

national standards should apply, without distinguishing between public and private sector schemes.

'Members' interests to be paramount'

46. SA Superannuants asserts that:

> Where an action being contemplated by a superannuation scheme trustee could deliver an advantage either to members or to some other party, such as an employer, and there is no specific authority to consider giving the advantage to the other party the advantage must go to scheme members. This is because of the specific obligation of trustees to act in the best interests of its beneficiaries.[39]

47. SA Superannuants goes on to suggest that 'instead of inserting the rules 29(4) and 29(5) for reducing pensions the Treasurer might have inserted [a] different rule',[40] which would have had the effect which they seek. As with other possible alternative drafts proposed by SA Superannuants, I consider this speculative and not relevant to a construction of the effect of clause 11. Whilst the Treasurer might have so acted, in the event he chose not to; and my task is to consider clause 11 as it exists, not as SA Superannuants would wish it to be.

48. Whilst I agree that a trustee has an obligation to act in the interests of the beneficiaries of a trust, in this case the EISS Board has an overriding obligation to apply the scheme rules. This obligation cannot be set aside by an expressed wish for the scheme to be administered in a way which delivers additional benefits to members, if administration in that way is not authorised by the scheme rules.

Protections for EISS members

49. Finally, whilst the policy question of whether the variation of the scheme rules **should** have had the effect of reducing employer costs is beyond my jurisdiction, I note that a number of elements in the legislative scheme were designed to protect the interests of EISS members. In my view these factors are relevant in considering whether clause 11 should be given the interpretation which I have proposed above.

50. The elements are:
    - the protection of the interest of members was afforded by the obligation to ensure that they were no worse off[41]
    - subclause 11(2) explicitly contemplated that a variation could be made to ensure that costs to employers were not increased[42]
    - the 2002 memorandum states that as part of the privatisation process, the Treasurer indicated to the tenderers that he would vary the rules so as to avoid an increase in employer costs, to the extent permitted by the constraint contained in clause 11.[43]

Did the Treasurer properly consult the EISS Board?

51. Under clause 11(1) of Schedule 1 to the Electricity Corporations Act, the Treasurer was obliged to consult with 'the trustee of the scheme' (i.e. the EISS Board) before making rules relating to changes in member benefits etc. following the scheme's loss of

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[39] SA Superannuants, *An argument against the proposition does not preclude a reduction in employer costs*, 14 January 2014, p6.

[40] SA Superannuants, *An argument against the proposition does not preclude a reduction in employer costs*, 14 January 2014, p6.

[41] See subclause 11(3).

[42] I note that following the making of Rule 29 subclause (2) is a spent force. See advice provided to the EISS Board by P A McNamara QC, 7 December 2007, paras. 228.4 and 249.

[43] 2002 memorandum, p1.

constitutional protection. SA Superannuants asserts that there were administrative errors in this process.

52. SA Superannuants' principal contention is that 'the Board was merely a passive recipient of the new rules',[44] and that this was in breach of its obligation to be an active participant in the process leading up to adoption of rules for benefit reductions. SA Superannuants states that the EISS Board lacked 'the assertiveness required to adequately defend the interests of its beneficiaries'.[45]

53. However, I can see no basis for this contention. Under clause 11 the responsibility for making the scheme rules rested on the Treasurer, and before making the rules the Treasurer was obliged to consult with the EISS Board. This is a common legislative formulation to ensure that rules are not made without a relevant party having the opportunity to express a view about a proposal. But in my view it does not cast any obligation on the recipient of the benefit to take advantage of the opportunity. In my view the provision was intended as a limitation on the Treasurer's power.

54. I note also that the EISS Board is the trustee of the scheme. In my view, this role does not extend to 'defending the interests of its beneficiaries'. The EISS Board's role is to administer the scheme pursuant to the Schedule, the Trust Deed and the scheme rules.[46] This should be done in the interests of all parties who have an interest in it, not simply scheme members. This includes employers.

55. In the event, the then Treasurer wrote to the EISS Board on 2 July 2000 to advise that rules would be inserted into the scheme rules to reduce benefits following EISS's move into a taxed environment, and this was supplemented by correspondence from the Undertreasurer on 5 July 2000. On 29 May 2002, the EISS Board established a sub-committee to deal with the matter, but SA Superannuants asserts that at the EISS Board meeting held on 26 June 2002 the Board was still confused as to the workings of the tax reductions to benefits. The Chairman sought a further report to be provided to the July meeting of the EISS Board.[47]

56. Given that these events occurred 12 years ago, it is not now possible to state with any certainty what was in the minds of the EISS Board members at the time. Even if I accept the conclusions proposed by SA Superannuants as to the EISS Board's state of knowledge of the matter, I do not consider that this is evidence of administrative error. Clause 11 makes it clear that it was the Treasurer's responsibility to satisfy himself as to the matters set out there.

Was the 7 June 2002 letter misleading?

57. A related matter concerns a letter dated 7 June 2002, which appears on EISS Board letterhead, and which states that it is signed with the authority of the Secretary to the

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[44] Second SA Superannuants submission, p16.
[45] Second SA Superannuants submission, p17.
[46] Clause 3(1) of Schedule 1 to the Electricity Corporations Act.
[47] In relation to the Board's deliberations at this time, Mr Prior commented to my investigation as follows:

> I feel the need to make comment on this paragraph because I attended several of the EISS Board meetings during the period when the Board was considering the matter how and the extent of the benefit reduction that was to apply to member benefits. I can clearly recall the Board finding it difficult to understand the explanations that Allan Archer, as actuarial adviser to the Treasurer, was providing in justification for the formula reductions that he was recommending to the Treasurer. The Board was having difficulty in understanding the explanations because of the complex actuarial workings. I also clearly remember, the then chair of the Board, Mr Max Bray, making a comment along the lines; 'well whilst several members are still having difficulty In understanding all this, I guess at the end of the day the Treasurer is going to accept the advice of his actuarial adviser and so we as a board should endorse the proposed formula adjustment'. As I stated at our meeting, the Board's records about this time are probably 'a bit lacking' as it is my recollection that the period immediately before the benefit reduction formula was brought into operation, the secretary of the board became seriously Ill and the secretarial role was undertaken by several "stand in persons".

Board. In considering this letter I have accepted that it purports to represent the position of the Board on 'the proposed movement of the fund into the tax environment'.

58. SA Superannuants has asserted that there is no evidence that the EISS Board actually considered this letter; and that certain officers (including the then and current Chairman of the EISS Board, and its Chief Executive Officer) who would have been expected to know of its contents have no recollection of it. SA Superannuants assert that the letter was prepared by an actuary who worked at the time for Mercer; and who is since deceased. They imply that there is no factual basis for the letter's statement that the Board 'supports and recommends the proposed rule changes that have been developed by [the actuary]'.[48]

59. SA Superannuants has also suggested to me that 'there is a reasonable basis for suspecting that the letter is a false document in terms of the *Criminal Law Consolidation Act 1935 (Section 140 Dishonest dealings with documents)*'. I do not agree that there is any evidence to support a conclusion that there is some criminality attached to the preparation of the document. The offence created by section 140(4) of the Criminal Law Consolidation Act requires (in paragraph (b) of the subsection) proof beyond reasonable doubt of an intention to benefit the creator of a document, or to cause detriment to another. In my view there is simply no evidence of this element of the offence.

60. Further, in my view it does not follow that any doubt surrounding the authenticity of the letter amounts to evidence of an administrative error. In order to make a finding to this effect, I would need to be satisfied to the requisite degree[49] that such an error occurred. Whilst I consider it possible that the letter was sent without the express authorisation of the Board, or at least of a senior officer of the Board, I have no evidence - only conjecture - that the letter misrepresents the EISS Board's position.

61. I note also that even if I were to find an administrative error, that would have no practical effect on the decision made by the Treasurer to adopt the rules. The Treasurer's decision is beyond my jurisdiction, but I consider it likely that the letter written on behalf of the EISS Board was simply one element or factor taken into account by the Treasurer. I am not able to speculate as to its significance in that process.

Was the 2002 memorandum misleading?

62. Mercer prepared the 2002 memorandum to assist the Treasurer's consideration of the proposed rule changes. The memorandum states the purpose of the amendments as being:

> … to specify the way in which benefits from the Electricity Industry Superannuation Scheme should be reduced to allow for the Scheme being taxed with effect from I July 2000.
>
> In summary, the reductions to gross benefits payable from the Scheme are such that:
> - benefits after tax received by existing members will not be lower than would have applied had the Scheme remained untaxed;
> - employer costs are not expected to change as a result of the tax changes.

63. SA Superannuants asserts that the memorandum 'was not seen by the EISS Board beforehand'; and that this 'demonstrates s (sic) a lack of probity in the processes associated with its production and subsequent use as the sole basis for claiming that the rule changes would not have an effect on employer costs'.[50] It states that in

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[48] Second SA Superannuants submission, pp 7-10.
[49] In this situation, the Briginshaw principle outlined above applies.
[50] Second SA Superannuants submission, p10.

response to an application under the *Freedom of Information Act 1991* the department was unable to produce any documents commissioning the work that the memorandum purports to describe.[51]

64. SA Superannuants also asserts that 'there is a possibility that the actuarial adviser wrote an explanatory memorandum to a set of rule changes that Mercer had never been formally authorised to develop'.[52]

65. However, the department has provided me with a copy of a letter dated 4 December 2001, written by the Director, Superannuation (Policy) in the department to Mr Allan Archer, Principal, William M Mercer Pty. Ltd. The letter states:

> The purpose of this letter is to formally advise you that the Treasurer has appointed you to assist in advising the Treasurer in relation to the appropriate rule changes to avoid or reduce an increase in employer costs caused by changes in the incidence of taxation as a result of the EISS scheme's expected future loss of constitutional protection.

The department subsequently paid for the advice.[53]

66. In its response to my provisional report,[54] SA Superannuants questioned whether Mercer had been properly engaged to provide advice to assist the Treasurer. However, in my view, the 4 December 2001 letter demonstrates that Mercer was properly commissioned, and I can see no administrative error in this sequence of events.

67. SA Superannuants also claims that the department should have been aware that the memorandum was misleading in asserting that employer costs would be unaffected; and that the department was 'reckless' in accepting Mercer's conclusions without the evidence of worksheets detailing how they were obtained.[55]

68. In responding to my provisional report, Mr Prior commented as follows:

> This assertion is simply not correct as a copy of Mercer worksheets were provided as background material in the file that went before the Treasurer. … I can assure you that much more than a copy of the 2002 memorandum accompanied the minute that went to the Treasurer. In fact a very detailed copy of the actuary's workings went in the file to the Treasurer. EISS Board files, Treasury files and the ERSU files would (should) have a copy of the Mercer detailed workings, as there many copies produced and distributed as they were produced by a commercial printer.

69. SA Superannuants points to the fact that the departmental advice was dated 26 June 2002, and suggests that the proximity of this date to 28 June 2002, when the Treasurer made his decision to amend the rules, did not allow the Treasurer to reflect on the issues before making his decision. It also makes other criticisms of the content of the 2002 memorandum, which it states 'should have been recognised by Treasury as indicators that employer costs for pensions would be reduced by the method';[56] and which include the fact that the memorandum made no reference to a method or formula used in the other Australian jurisdictions to reduce pensions in response to taxes that became payable on superannuation fund income from 1 July 1988. SA Superannuants concludes that:

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[51] I have reviewed the scope of this FOI application, and I consider that the letter dated 4 December 2001 to which I refer below should have been provided in response to the application.

[52] Second SA Superannuants submission, p10.

[53] The SA Superannuants submission refers at p10 to an invoice which apparently relates to this work. It states that Mercer sent the invoice to the EISS Board , which forwarded it to the department for payment.

[54] I acknowledge that their response was prepared before SA Superannuants had an opportunity to consider the terms of the 4 December 2001 letter.

[55] Second SA Superannuants submission, p11.

[56] Second SA Superannuants submission, p11.

> The circumstances surrounding the production and use of the Explanatory Memorandum provide a reasonable basis for suspecting that Treasury and the actuarial adviser worked together to ensure that the Treasurer would have no opportunity to see the possibility that he was being advised to authorise use of a rule for reduction of pensions that was not valid.[57]

70. The 2002 memorandum was prepared to assist the Treasurer in his decision-making. As with the departmental advice and the 7 June 2002 letter purporting to be from the EISS Board, it was one of the factors which the Treasurer took into account in making his decision. Because the Treasurer's actions are not within my jurisdiction, I am not able to speculate about the significance of the 2002 memorandum in that decision-making process.

71. In summary, I do not see any administrative error in the department's advice to the Treasurer at this time. Mercer was an appropriately qualified body to provide expert advice on superannuation matters, and in my view it was not unreasonable for the department to rely on the expert advice which it commissioned to assist the Treasurer's decision-making. I do not consider that the department was under an obligation to 'second guess' the Mercer advice.

Was the effect of the proposed rule changes properly explained to the Treasurer in 2002?

72. The next substantive question is whether the effect of the rule changes was properly explained in the advice provided to the Treasurer by the department and the EISS Board in May 2002 when the new rules were made. In considering this question I have had particular regard to the departmental advice; the 2002 memorandum; and the 7 June 2002 letter purporting to be from the EISS Board.

73. The departmental advice quoted clause 11 in full, and continued:

> The "relevant day" under subclause (6) is defined to be the day on which the approval of the Treasurer ceases to be required for the variation or replacement of the Rules. In terms of a notice already issued by the Treasurer, the "relevant day" is 30 June 2002.
>
> Mr Allan Archer, Principal with Mercer Human Resource Consulting, who was appointed by the former Treasurer to assist in advising the Treasurer in regards to the proposed rules to be inserted under Clause 11, has prepared a set of draft rules which reduce member gross benefits in the Electricity Industry Superannuation Scheme in a manner which provides for member net after tax benefits to remain the same, while at the same time maintaining the same level of employer support to the superannuation scheme.
>
> Both John Barrett (Actuarial Analyst) and myself have had extensive consultation with Mr Archer in relation to these draft rules and we are satisfied that the proposed rules meet the intentions of the legislation and also satisfy the guarantees provided to members by the legislation.
>
> As required by subclause (1) of Clause 11 of Schedule 1 of the *Electricity Corporations Act*, the trustee of the scheme (the Electricity Industry Superannuation Board) has been extensively consulted in relation to the proposed rule change. The proposed rule change has been "endorsed" by the Board.
>
> It is therefore recommended that in accordance with subclause (6) you issue a notice to the Electricity Industry Superannuation Board the effect of the notice being the insertion into the rules of the Electricity Industry Superannuation Scheme, the Variation to the Rules as set out in the attachment to this minute.
>
> A draft letter, in the form of a notice to the Electricity Industry Superannuation Board has been prepared for your signature.

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[57] Second SA Superannuants submission, p12.

It is also recommended that you initial each page of the Variation to the Rules.

[Signed]
D R Prior
DIRECTOR, SUPERANNUATION (POLICY)
26 June 2002

[Approved]
Kevin Foley MP
TREASURER
28 June 2002

74. I have considered whether there is any administrative error in this advice, and in particular in the statement that the new rules 'reduce member gross benefits in the Electricity Industry Superannuation Scheme in a manner which provides for member net after tax benefits to remain the same, while at the same time maintaining the same level of employer support to the superannuation scheme'. I have concluded that, based on the Mercer advice, there were reasonable grounds for the making of that statement.

75. I have also considered the nature of some specific comments in the 2002 memorandum. It states firstly that as from 1 July 2000, benefit payments from the EISS had been 'reduced on account of taxation on an interim basis', and paid out as benefits paid from a taxed source. This action was taken with the knowledge of Commonwealth and state treasuries, and arose from the delay by the Commonwealth in ceasing the constitutional protection while it waited to pass legislation to impose tax at the time of the loss of constitutional protection.[58]

76. The 2002 memorandum outlines the assumptions upon which the interim benefit reductions were calculated. It states, and I accept, that these assumptions were conservative, and led to the lowest practical level for the benefit reductions. The 2002 memorandum states that in practice, many members would have ended up with higher net benefits because their individual situations were more favourable than assumed.

77. In relation to employer costs, the 2002 memorandum summarises the actuarial advice and concludes:

> This result indicates that an increase in employer costs will be avoided if the Treasurer reduces benefits to the maximum extent permitted under legislation (given the assumptions above). The outcome for members is that they will receive at least the same benefits after tax as they would have received had the Scheme remained untaxed. The proposed rule amendments provide this outcome.

78. On the face of this documentation, I consider that there were reasonable grounds for the making of these statements, and I can see no shortcomings in this advice. I acknowledge that there is contention as to the subsequent effect of the rules in relation to employer costs, but as I note elsewhere, this fact is not of itself sufficient to demonstrate an administrative error. In my view there is simply not sufficient evidence to substantiate any finding of error based on inadequacy of the 2002 memorandum.

The 1998 memorandum

79. SA Superannuants asserts[59] that the advice in the 2002 memorandum is inconsistent with advice provided in an earlier memorandum prepared by Mercer dated January

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[58] Explanatory memorandum, p2.
[59] Second SA Superannuants submission, p12.

1998.[60] I have not been provided with a complete copy of this document, but I have had regard to an extract provided by SA Superannuants.[61]

80. I note firstly that the 1998 memorandum refers to the whole state pension scheme, not simply the EISS. It is my understanding that there was significant difference between the two schemes,[62] arising from the taxation treatment of the movement of assets to support existing pensions. At the relevant time there were no existing pensioners for the EISS scheme, as they had all been moved to the wider state scheme.

81. In summary, the extract from the 1998 memorandum states that the PJFC would be available to reduce tax on employer contributions in relation to the pension environment (though not the lump sum environment), through the application of the PJFC to what is known as the pre June 1983 component of a pension. It states that 'the extent of cost reduction across the whole Pension Scheme could be very large'; notes that there are a number of factors which mean that the whole PJFC could not be applied 'straightaway'; and concludes that 'its size is such that multi-million dollar savings to the Government in present value terms may be feasible'.[63]

82. The 1998 memorandum includes the following comment:

> 19.23 The Government may need to cope with demands from members of the Pension Scheme that they, as well as the Government, should share in the gains achieved. An important part of the response would be that these people are still members of schemes which have been closed because of their generosity, and yet their benefits have been continued. Thus they should have little to complain about if the advantage of applying the PJFC is not passed through to them, so long as they are not detrimentally affected. A critical point is that the benefit reductions should be such as to remove the windfall gains, but not to the extent of causing detriment to any members.

83. The 2002 memorandum, which refers only to the EISS not the whole state pension scheme, contains the following statement in relation to the PJFC:

> **Pre July 1988 Funding Credit**
>
> At the end of May 2002, the Scheme received from APRA confirmation of a Pre-July 1988 Funding Credit, which allows tax credits on account of the unfunded nature of the Scheme when superannuation funds in general become (sic) taxed in July 1988. The extent to which these tax credits can be utilised each year depends upon whether employer contributions paid to the Scheme in that year exceed the sum of the post 1983 part of the taxed benefits paid by the Scheme over the year.
>
> The actuary has estimated that these credits are worth around $25 million (in present value terms) to the Scheme.

84. I do not see any inconsistency between the statement in the 1998 memorandum that the PJFC would be available to reduce tax on employer contributions for the state pension scheme, and the statement in the 2002 memorandum that the PJFC would result in credits to the EISS. It appears to me that the import of the statements in both documents is that the PJFC would be of benefit in reducing the employer funding costs. The 2002 memorandum includes an actuarial estimate of that benefit to the EISS because the extent of the available PJFC had been confirmed by the Australian Prudential Regulation Authority at that time.

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[60] Department of Treasury and Finance, *Study of the Taxation Status of the SA Government Superannuation Funds*, Prepared by William M Mercer Pty Ltd, Allan Archer, Principal; Tony Cole Worldwide Partner; John Ward, Principal.
[61] Part 19 The Pension Scheme pp. 59-61. See First SA Superannuants submission, p7 and Attachment 2.
[62] i.e. apart from the fact that they operate under different legal frameworks.
[63] Paragraphs 19.20 to 19.21.

The 2004 memorandum

85. SA Superannuants asserts also that the 2002 memorandum is inconsistent with a 2004 memorandum also prepared by Mercer.[64] Again I have relied on an extract from that document provided by SA Superannuants.[65]

86. I infer from the covering letter to the extract of the 2004 memorandum that, like the 1998 memorandum, the 2004 memorandum addresses taxation issues relevant to the broader state superannuation schemes; rather than simply the EISS.

87. In addition, the 2004 memorandum post-dates the 2002 memorandum, and thus it could be expected that it would be able to draw on post-implementation experience in outlining the effects of moving the EISS to a taxed status. SA Superannuants contends that the content of the 2004 memorandum should have alerted the department to the alleged deficiencies in the 2002 memorandum, and the fact that employer costs had been reduced as a result of the variation of the scheme rules.

88. I acknowledge that the extract from the 2004 memorandum does not refer to the 2002 memorandum. In my view this is not surprising given that the two memoranda were dealing with different schemes. Further, the 2004 memorandum in my view is broadly consistent with the statements made in the 1998 and 2002 memoranda. I note in particular the following comment, which is referring to the broader state superannuation schemes rather than the EISS:

> In the Lump Sum/Pension Scheme there is a net tax advantage in moving from an untaxed environment to a taxed environment. These advantages could be used to increase members' benefits and/or reduce employer costs. If members' benefits are maintained at current levels (after allowing for tax effects), then savings of the order of $450 million are estimated for the employer.[66]

89. In summary, I consider that the departmental advice and the 2002 memorandum provided a reasonable explanation upon which the Treasurer could rely in making his decision. I note in particular that:
    - Mercer was at the time acknowledged as an expert adviser in superannuation fund management
    - the 2002 memorandum correctly states the obligations under clause 11; namely to ensure that benefits after tax must not be lower than would have applied had the EISS remained untaxed; and that any rise in employer costs as a consequence of the changes should be avoided
    - it provides apparently authoritative advice on the key issues to be considered
    - it based its advice on conservative and reasonable assumptions to ensure that members were not disadvantaged
    - the assumptions were themselves based on 2 years' experience in operation as interim arrangements
    - consistently with the 1998 memorandum, it acknowledges that the PJFC would result in credits to the EISS
    - it is not inconsistent with the advice provided by Mercer in the 2004 memorandum about taxation issues relevant to the broader state superannuation schemes.

90. It may be that as SA Superannuants asserts, time has proven some of the 2002 memorandum's actuarial predictions not to be fully realised; or to be incorrect. However, any predictive actuarial calculation must of its nature have an element of doubt, and the simple fact that some predictions have not been fulfilled exactly as may

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64 Department of Treasury and Finance, *Review of Taxation Status of the SA Government Superannuation Funds*, prepared by Mercer Human Resource Consulting, 23 December 2004.
65 Page 7, and Appendix A pp. 9-10. See First SA Superannuants submission, p8 and Attachment 5.
66 Page 7.

have been anticipated does not imply that there is an administrative error in the original advice.

91. I have noted above that I do not see evidence of any administrative error to support SA Superannuants' claim that the department should have been aware that the memorandum was misleading in asserting that employer costs would be unaffected; and that the department was 'reckless' in accepting Mercer's conclusions. I have noted also Mr Prior's clear recollection that the Treasurer was provided with the worksheets detailing how the conclusions were obtained.

Was the Treasury – Mercer relationship inappropriate?

92. SA Superannuants next contends that 'the actuarial adviser and Treasury [worked] together to exploit [the lack of assertiveness] of the EISS Board and put in place a set of rules that should have been subject to much closer scrutiny than they received'.[67] It contends that in the 1998 memorandum,[68] Mercer through the actuarial adviser 'expressed a view that in any shift of the State Pension Scheme to the taxed superannuation environment members should make no gains from the change and the intrinsic advantage of paying the pensions from the taxed environment should be passed to employers'.[69]

93. SA Superannuants contends that there is no legitimate basis for the view expressed in the 1998 memorandum that gains made by members could be regarded as 'windfall gains', which should be removed and transferred to employers. It contends that this is a wrong view because the Australian superannuation system is designed to provide taxation gains to members, not to employers. It contends that this expression of view should have excluded Mercer, and the three authors of the 1998 memorandum, from providing advice to government on the matter of the rule changes.[70]

94. As a matter of administrative law, there is no basis for SA Superannuants' contentions insofar as they relate to the role of Mercer and the actuarial adviser in the decision to vary the scheme rules. This is because questions of apprehended bias can only arise where a decision which affects the legitimate expectations of the person interested is made by a decision-maker. In this case, Mercer and the actuarial adviser were not acting as decision-makers. As I have outlined above, that responsibility sat with the Treasurer.

95. Further, I do not consider that any question of a perceived conflict of interest on the part of Mercer can arise. Whilst I acknowledge that SA Superannuants does not like the views expressed by Mercer, as being inimical to their interests, those views were nonetheless legitimate public interest considerations in the decision-making process. The department would have been remiss had such matters not formed a part of the advice given to the Treasurer at the time.

Have the rule changes resulted in reduced employer costs?

96. Although it is my view that there is nothing in the EISS framework which precludes a reduction in employer costs, it could be argued that a 'windfall' gain such as that which accrued to the scheme as a result of the application of the PJFC should not accrue solely to employers, but should be shared between employers and members.

97. I note also that it appears to me that SA Superannuants may have been given a verbal assurance that net savings arising from the tax status changes would be passed on to

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[67] Second SA Superannuants submission, p17.
[68] I quote a relevant section from the 1998 memorandum below.
[69] Second SA Superannuants submission, p18.
[70] Second SA Superannuants submission, p18

members. In a letter dated 31 March 2006, sent to the then Treasurer by the Secretary of SA Superannuants, Mr Vic Potticary, the following passage appears:

> When Association President, Ray Hickman, Vice-President Clive Brooks and I met with you and Mr Deane Prior (a Treasury official) on 1 December, 2005 we reported back to the Association Executive Committee that the Labor Government would only seek to ensure that any change in pension scheme tax status was cost neutral for the Government and that net savings would be passed to members. Our report was based on the notes we made immediately after the meeting.
>
> If the Labor Government supports the principle that net tax savings should pass to members when a pension fund moves to the taxed environment we do not know what to make of the fact that the EISS is passing all tax savings to employers instead. **Is this happening without the current Government's knowledge or support?** (emphasis in original)

98. On the question of whether employer costs have in fact reduced, SA Superannuants maintains that this is demonstrated by:
    - the 'arithmetic certainty' that EISS assets would have been depleted by much less than 15%
    - the alleged deficiencies in the 2002 memorandum
    - the 1998 and 2004 memoranda
    - the annual taxation experience of EISS between 2000 and 2006
    - a series of reports dated 23 March 2003 provided by Mr Archer to the EISS Board concerning different parts of EISS related to different employers
    - the 30 June 2011 actuarial investigation of EISS
    - the alleged deficiencies in the response given by the Hon Michael O'Brien MP, Minister for Finance, to a question by the Shadow Treasurer, the Hon Iain Evans MP, in 2012.[71]

99. On the same issue, the EISS Board has advised me as follows:

> **Pre-July 1988 Funding Credits (PJFCs)**
>
> 68. A PJFC is a Pre-July 1988 Funding Credit. This allows employer contributions in respect of the unfunded liability for pre-1988 benefits to be untaxed for a taxed fund. This was a large part of the actuarial analysis on rules 29–31.
>
> 69. The PJFC of $258m shown in the extract from the minutes of May 2002 is far more than would be expected to use (sic). Also, this does not represent the value of the PJFC to the Scheme. This amount allows $258m worth of contributions to be non-taxable. That is, the maximum value of the PJFC to the Scheme is the tax on $258m worth of contributions, or 15% of $258m, i.e. $38m.
>
> 70. The value of PJFCs allowed for in the actuarial analysis in the explanatory memorandum for the tax offset rules is $25m. That is, the Scheme was assumed to claim $166m worth of employer contributions against its PJFC (15% of $166m is $25m).
>
> 71. In 2003-2005, the value of the tax saved by the PJFCs claimed to date was around $20m. In 2005/06 no PJFCs were claimed, and following the 2007 tax changes, the Scheme has stopped claiming PJFCs.
>
> 72. The value therefore to the Scheme of actual PJFCs claimed was less than was estimated in the actuarial analysis for the tax offset rules.
>
> 73. PJFCs have been allowed for on a scheme-wide basis in the calculation of the "employer cost test". The nature of the credit makes it difficult for this amount to be allowed for on an individual member-by-member basis.

[71] See First SA Superannuants submission, pp 6-10.

Summary

74. The tax offset rules were made because the Scheme's loss of constitutional protection imposed a tax liability on the Scheme. This would have increased employer costs and provided a windfall benefit to members without a reduction in gross benefits. The EC Act allowed for this increase in cost to be minimised.

75. The tax offset rules were inserted by the Treasurer into the Scheme rules in June 2002 pursuant to his powers under clause 11 of the EC Act, following consultation with the EISS Board.

76. The rules required that members' net benefits from a taxed fund would be equal to those from an untaxed fund, under three major assumptions regarding the payment of benefits.

77. The actuarial analysis in the explanatory memorandum is that the reductions imposed by the rule changes, as well as the use of the Scheme's PJFC, are sufficient to pay the extra tax liability caused by the Scheme's loss of constitutional protection. That is, on a scheme-wide basis, employer costs were expected to be unchanged.

78. There was significant consultation between Treasury, Mercer and the EISS Board on the tax offset rules between 2000 and 2002.[72]

100. In its response to my provisional report, SA Superannuants questioned the value of the tax savings made by EISS through its use of PJFCs. It commented:

Advice given to you by the EISS Board on the matter of the value of the tax savings made by EISS through its use of pre-July 1988 Funding Credits (PTFCs) was that the value was 'around' $20 million … For this to be true the amount of PJFC utilised has to be 'around' $133 million (15% of$l33 million is $20 million).

In our submission of January 2014 on page 15 we claimed that the tax savings to EISS from its utilization of PJFCs was $36 million. This estimate was obtained by calculating 15% of $238 million which was the total amount of PJFC utilised by EISS up until 30 June 2005. We provided you with Attachment 27: Page from 2005 £155 Financial statement confirming amount of PJFC utililised as proof of the validity of the $238 million figure. $36 million is $11 million more than estimated in the Explanatory memorandum and $16 million more than the EISS Board has advised you was actually achieved.

We request that you refer the EISS Board to its 2005 Annual Report and ask it to reconcile its statement in your numbered point 96 that 'In 2003-2005, the value of the tax saved by the PJFCs claimed to date was around $20 million.' with the amounts of PJFC utilization set out in the 30 June 2005 Annual Report.

101. I put this matter to the EISS Board, which responded as follows:

We refer to your email of 17 June and your question on our submission to your inquiry into aspects of the Electricity Industry Superannuation Scheme.

Our calculation of the value of the tax savings from the use of PJFCs was based on nominal value of the tax credit for the financial years 2003-2005. The value of credits for the financial years 2001 and 2002 was inadvertently left out of our calculation. The total nominal value of the tax credits claimed by the Scheme has been $36m.

We would draw your attention to the statement by the SA Superannuants that "$36m is $11m more than estimated in the Explanatory memorandum" and respectfully suggest that this comparison is not appropriate.

The value of the PJFC tax credits allowed for in the Explanatory Memorandum of $25m is a present value based on actuarial assumptions. We understand that this present value was

[72] EISS Board submission, p11.

> calculated as at 1 July 2000. The $36m figure quoted is a nominal value, ie a simple sum of the amounts claimed over 5 financial years.
>
> When the present value at 2000 of the tax credits actually claimed over the 5 years – allowing for the late submission of the 2001 and 2002 tax returns and using a discount rate of 8% - is calculated, the value is approximately $26m.
>
> Whilst slightly higher than the value of $25m in the Explanatory Memorandum, we consider that the difference is not material in the overall context of the Explanatory Memorandum.
>
> We use a discount rate of 8% in this calculation as we understand that this is the untaxed discount rate used for the advice to the Treasurer.[73]

102. In oral evidence given to me, the EISS Board Chief Executive Officer (a qualified actuary) stated that it is not practically possible today to quantify the impact of the 2002 rule changes on employer costs. However, it is his view that there is no doubt that employer costs have risen since 2002, due to a range of factors which include fewer pension commutations; longer life expectancies; fewer resignations; and salary increases being higher than expected. He gave evidence that this view is certainly shared by the employers.

103. In these circumstances, it is not possible for me to reach a concluded view on whether employer costs were actually reduced as a result of the tax offset implementation, without a detailed historical and actuarial analysis; and it is unlikely that such an analysis will produce a clear result. In view of:
    - the fact that it is a policy decision as to whether net savings should be passed on to members or used to off-set employer costs
    - the preliminary conclusion which I have reached - namely that the legal framework did not preclude a reduction in employer costs
    - the time which has elapsed since the original decisions were made

    I do not consider that further investigation of this issue by me is warranted.

104. Finally, I note that the EISS Board is now responsible for the scheme rules, and may, by instrument in writing, vary or replace them.[74] However, where an increase in employer costs would result, the approval of the employers is required.[75] It appears to me that it is now a matter for the Board to consider whether it is appropriate to adjust the scheme rules to deal differently with this issue; and I note that in August 2007 it requested employers to consider a cap on the tax offset on pension benefits. This request was rejected.

Opinion

I do not consider that any administrative error occurred in connection with the changes to the scheme rules made on 28 June 2002.

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[73] Email from the EISS Chief Executive Officer, 27 June 2014.
[74] Clause 4(1) of the Trust Deed.
[75] Clause 4(4) of the Trust Deed.

Whether the department misled the Crown Solicitor in seeking legal advice in 2007

105. For a considerable period of time, SA Superannuants has asserted that the rules do not comply with clause 11 of Schedule 1 to the Electricity Corporations Act. They have raised their concerns in a number of ways, including with the EISS Board. As a consequence of those concerns, the EISS Board Chairman wrote to the Treasurer on 2 August 2007. The department provided advice to the Treasurer in relation to this correspondence in a minute dated 28 November 2007.

106. In order to prepare the 28 November 2007 minute, the department sought advice from the Crown Solicitor on whether the rules complied with clause 11.[76] Through the advice provided by Mr McDonald on 26 November 2007,[77] the Crown Solicitor advised that they did comply. However, SA Superannuants asserts that the Crown Solicitor was misled in forming his opinion, because the department provided only a copy of the 2002 memorandum; and not copies of the 1998 and 2004 memoranda from Mercer on the broader state pension schemes.

107. The Crown Solicitor's advice was sought by Mr Prior by memorandum dated 4 September 2007. The memorandum is as follows:

> On 6 August 2007, the Treasurer received correspondence from the South Australian Government Superannuated Employees Association Incorporated (SA Superannuants), arguing that the rules the Treasurer inserted into the EISS on 28 June 2002, were invalid. A copy of the relevant rules and the explanatory memorandum are attached to this minute.
>
> As background to why SA Superannuants have an interest in this matter when their members are former public servants and not former electricity industry employees, I can advise you that the interest comes from trying to second guess how the government might choose to reduce the gross benefits of pensions paid to retired public servants if the government decided to move the SA Superannuation Fund into the taxed environment. I must advise you the government has no plans at this time to pay pensions from a taxed source. SA Superannuants have been advised on numerous occasions that if a decision were made to pay State Scheme pensions from a taxed source, they should not assume that the reduction in gross pensions to offset the increased cost to the government (from the fund having to pay contributions tax and investment earnings tax) would be undertaken in the same manner. This has not stopped them from arguing that the rule change for the EISS scheme was invalid, as a means of trying to ensure that such an approach not even be considered for the State Scheme. We believe that by stating the rules are 'invalid', they really mean the rules are more 'unfair' than not legal. This is because the rules reduced pensions such that the amount of the net after tax benefit of the pension paid from an untaxed arrangement was the same as the net after tax benefit received from the pension paid from a taxed arrangement. The concern is that tax rates have changed since the rule was introduced.
>
> SA Superannuants argue that the rules inserted in terms of Clause 11 of Schedule 3 of the *Electricity Corporations Act 1994* [as inserted by Part 2 of Schedule 3 of the *Electricity Corporations (Restructuring and Disposal) Act 1999*], are invalid because the new rule reduced member gross benefits under the taxed fund arrangement to the maximum extent permissible in terms of the *Electricity Corporations Act*, and thereby reduced employer costs of the scheme. The rule inserted into the rules of the scheme ensure that retiring members will have the same net after tax benefit from the taxed fund as the net benefit they would have received if the benefit had been paid from an untaxed source. The legislation guaranteed that member benefits would not be less than this net benefit.
>
> The rule was recommended by the actuary (the late Allan Archer) who was at the time advising the Treasurer, and also recommended by the Trustees and the lawyer advising the Trustees, Ms Suzanne MacKenzie.

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76 I note that the department had previously sought advice on a related issue from the Crown Solicitor. This advice was dated 25 January 2006, and is referred to above.

77 This advice is described in paragraphs 35-37 above.

[Clause 11 is then quoted in full]

This matter has been raised with Crown Law previously, and I refer to your advice of 25 January 2006, prepared by Mr Chad Jacobi. A copy of this previous advice (reference CSO:0067695) is attached to this minute.

In responding to the recent letters from SA Superannuants, the Treasurer has advised that the rule changes are 'not inconsistent' with the provisions in Part F of Schedule 1 of the Electricity Corporations Act. This position is based on previous interpretation of the powers provided under Clause 11 of Part F, and previous legal commentary from both the lawyer advising the EISS Board and Crown Law.

However, as SA Superannuants have come back again and are still arguing that the rule change was not 'valid', we seek a confirmation of your opinion that the rule changes were legal.

Copies of the recent exchange of letters between SA Superannuants and the Treasurer are also attached.

108. SA Superannuants contends that:

… the Treasury case that the rule changes of 2002 had a sound basis in law has always been flimsy. The quality of the Crown Law advice that all rule changes are entirely valid can be no better than the quality of the calculations used to generate the values contained in the Explanatory Memorandum.[78]

109. I consider that this statement is misconceived. As outlined above, I agree with the Crown Solicitor that the rules were validly made. In my view, there was no legal obligation requiring that the rules should not reduce employer costs.

110. SA Superannuants has advised me that on 25 May 2012, the Hon Iain Evans MP sent a letter to the Minister for Finance, in connection with this issue. He asked the following question:

Is the Minister aware that the 1998 and 2004 Mercer reports were not provided to the Crown Solicitor when he was directed to provide his opinion on the validity of the EISS method for calculating taxed-source pensions. He was provided with an Explanatory Memorandum, dated 27 June 2002 and written by a co-author of the 1998 Mercer Report which, in conflict with that report, expressly stated "employer costs are not expected to change as a result of the tax changes." Does the Minister agree that the Crown Solicitor should now be provided with a complete brief?[79]

111. SA Superannuants advises that the Minister responded:

I am advised that (and for the reasons given in the response to the previous question) the 1998 and 2004 Mercer Reports were not relevant. The Explanatory Memorandum relates to the EISS scheme specifically. I am advised that there is no conflict between the statements made in the EISS Explanatory Memorandum, and statements made in the Mercer reports dealing with the main State Superannuation Scheme. The differences in the outcomes in respect of the two schemes can be explained by the following:

- As at the dates that Mercer Investigated the implications associated with the main State Superannuation Scheme moving into the taxed environment, the employer liability in respect of existing pensioners was significantly under funded. Therefore, there would have been significant tax benefits to be gained in funding those employer liabilities in a managed manner over a period of many years to gain the maximum advantage.

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78 Second SA Superannuants submission, p23.

79 I have sought copies of this correspondence from SA Superannuants, who advised me that it would be provided to me by Mr Evans' office. At the date of preparing this provisional report, this has not occurred; but I note that the exchange of correspondence was referred to, but not directly quoted, in debate on the *Statutes Amendment and Repeal (Superannuation) Bill 2012* - see *Hansard*, 30 May 2012.

- As at the dates that Mercer investigated the implications associated with the main State Superannuation Scheme moving into the taxed environment, the employer liability in respect of the already accrued but not yet payable pension liabilities was significantly under funded. Therefore, there were tax benefits to be gained over time in finding those past service liabilities.
- Furthermore, there were no existing pensioners in the EISS scheme at the date the scheme moved into the taxed environment, as they had all been transferred to the State Scheme.[80]

112. SA Superannuants, in its second submission to me, acknowledge that these statements are correct, but do not agree that the 1998 and 2004 Mercer memoranda are irrelevant to EISS. It says:

> All three of the dot points above are correct statements but they do not support the position that the Mercer Reports of 1998 and 2004 are irrelevant to EISS. **The second dot point outlines a characteristic that EISS shared with the State Pension Scheme.** The difference in outcomes of applying the EISS method to the State Pension Scheme, as opposed to EISS, is not that savings were to be made in the first case and not the second. The three dot points taken together mean that **savings were to be made in both cases** with the only difference being that for EISS, the savings were made from pensions that commenced after the scheme shifted to the taxed superannuation environment. The savings must have been used to reduce employer costs for EISS pensions because members gained nothing.
>
> It does not matter if a pension scheme, at the time of its transfer to the taxed environment, has no pensioners, or has some members who are pensioner, or has all its members who are pensioners, and nor does it matter if the pension scheme is fully funded, or partly funded or entirely unfunded. In all these circumstances the EISS method for calculating pensions, after the transfer, will reduce employer costs for the pensions compared to what the cost would be if the scheme had not moved to the taxed environment. The only qualification that has to be made here is that the pension scheme must have a significant proportion of members with substantial amounts of pre 1 July 1983 service. **EISS had a large proportion of its pension division members in this category and whoever provided Mr O'Brien with the answer to Question 7 would know this**. (emphasis in original)

113. SA Superannuants also states that in responding to its representations, former Treasurer Foley had not previously asserted that the 1998 and 2004 memoranda were irrelevant, and that all he had done was to suggest that SA Superannuants' 'interpretation of Section 11(2), Part F of Schedule 1 *Superannuation* of the Electricity Corporations Act 1994 was incorrect'.[81]

114. The Minister's correspondence is beyond my jurisdiction. However, to the extent that it relies on advice provided by the department I consider that it represents a reasonable response to the assertions made by SA Superannuants.

115. Further, I do not see any administrative error in the department choosing not to provide the 1998 and 2004 memoranda to the Crown Solicitor. For the reasons outlined above, I accept that these two memoranda concerned the broader state scheme, and that different considerations applied to the EISS.

116. As noted above in relation to my jurisdiction, I am not able to investigate an administrative act done by a person in the capacity of legal adviser to the Crown or an agency to which the Ombudsman Act applies.[82] Consequently I am not able to investigate the advice provided to the department by the Crown Solicitor.

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[80] For the reason outlined in the previous footnote, I have not sighted this correspondence, and I rely on SA Superannuants' description of it.
[81] Second SA Superannuants submission, p24.
[82] See paragraph (d) of the definition of 'administrative act' in section 3 of the Ombudsman Act.

117. Nonetheless, I observe that the assertion by SA Superannuants that the Crown Solicitor was misled suggests that the Crown Solicitor was not able to determine for himself the facts necessary in order to provide the requested advice. Based on my reading of Mr McDonald's advice, I see no reasonable basis for this suggestion.

118. I note also that SA Superannuants has advised me that it took up an earlier proposal which I made to it, that it should ask the Crown Solicitor whether he considers that he was misled. The response to that request[83] indicates that the Crown Solicitor did not consider this to be the case. However, SA Superannuants asserts in its response to my provisional report that it believes this response refers to the advice given on 25 January 2006 by Mr Jacobi about clause 11(3); rather than advice given by Mr McDonald on 28 November 2007 about clause 11(2).

119. I see no reason to interpret the Crown Solicitor's response as being limited in this way. SA Superannuants provided me with a copy of this response. The substance is contained in the following paragraphs:

> I have reviewed the matter and I note your concern that my office was not adequately instructed when it advised the Department about the method of calculating superannuation pensions under the Electricity Corporations Act 1994. As you will appreciate, any advice that was provided was privileged and the Department does not propose to waive that privilege.
>
> I can assure you, however, that I am satisfied that no fraud has been perpetrated upon the Crown Solicitor in relation to this matter. Further, I am of the view that the nub of the Association's concern lies in an interpretation of the effect of clause 7 (sic) of Schedule 1 of the Act. That provision did not have the effect of limiting the Treasurer to the making of rules, in an ambulatory sense, that would result in no net detriment to superannuants. The obligation as properly construed as one that is satisfied at the point in time that the entitlement is calculated. I think that this reveals that the underlying difference between the Association's position and that of the State is one of statutory construction and not of actuarial calculation.

Opinion

I do not consider that the department misled the Crown Solicitor in seeking legal advice in 2007.

83 Letter from the Crown Solicitor to SA Superannuants dated 27 June 2013.

Whether since 2002 the department or the EISS Board has provided misleading advice in connection with the Treasurer's decision on the method used by EISS to calculate its taxed-source pensions

120. The final issue is whether the department or the EISS Board has subsequently provided misleading advice when SA Superannuants has raised its concerns about the effect of the rule changes.

121. At Appendix A is a document provided by the EISS Board which outlines the principal events with which the EISS Board has been involved since concerns were first raised about the tax offset issue in 2004.

122. In addition, SA Superannuants has drawn attention to the issue in other ways, including correspondence with Members of Parliament. At various times it has expressed concern about departmental and EISS Board advice provided in connection with the following matters:
- correspondence between the EISS Board and an EISS member, Mr Barry Foster, including:
    - materials provided to Mr Foster by the EISS Board at the time of his retirement at the end of 2002
    - letters dated 25 March 2006 and 18 May 2006 from Mr Foster to the EISS Board
    - responses from the EISS Board to Mr Foster dated 2 May 2006 and 28 September 2006
- the commissioning and receipt of the 2004 memorandum. I have dealt with this matter above, and concluded that I see no administrative error
- the release in 2006, following an application made under the Freedom of Information Act, of the 2004 memorandum. SA Superannuants contends that the department made a statement on the release of the report which pointed out that it had not been the subject of any consideration by government; and that this caution should be contrasted with the standard applied in the preparation of the 2002 memorandum
- a letter to the Treasurer dated 31 March 2006, and the response from the Acting Treasurer dated 12 October 2006. SA Superannuants criticises this response as being 'a communication of low probity.'[84] It is a Ministerial communication which is beyond my jurisdiction
- a letter and paper dated 6 December 2007 sent to the EISS Chairman, to which SA Superannuants states it received no response
- a letter sent to the EISS Chairman by the Australian Services Union, dated 31 May 2007; and a response dated 1 August 2007 and its attachments
- a letter sent to the Treasurer by the EISS Chairman, dated 2 August 2007 seeking a review of the rule amendments made in June 2002; and the Treasurer's response dated 13 December 2007
- a letter dated 26 May 2008 sent to SA Superannuants by the Treasurer, indicating 'that he had chosen not to respond to further questions from them concerning EISS'[85] because he had received Crown Law advice that the rule changes made in 2002 were entirely valid
- a letter dated 19 June 2008 sent to Hon Bob Such MP concerning one of his constituents Mr Richard Vear, which indicated that the department did not have copies of worksheets underpinning the 2002 memorandum. I have dealt with this issue above
- a letter sent to the EISS Chairman by the Australian Services Union, dated 15 July 2008; and a response dated 18 September 2008 sent by a solicitor acting on behalf of the EISS Board

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[84] Second SA Superannuants submission, p23.
[85] Second SA Superannuants submission, p23.

- a letter and paper dated 11 September 2008 sent to the EISS Chairman, to which SA Superannuants states it received no response
- an undated letter sent by SA Superannuants early in August 2012 to the Minister for Finance, referring to a question asked by the Hon Ian Evans MP in the House of Assembly on 25 May 2012. I have quoted relevant sections of this correspondence above in connection with the seeking of legal advice from the Crown Solicitor, and indicated that I see no administrative error in relation to it
- a March 2013 letter sent to Super SA by SA Superannuants; and a response dated 26 September 2013. The response declines to answer the questions asked on the basis that the parliamentary referral seeking my investigation had been made. SA Superannuants speculates that 'Super SA was prevented from answering the questions because the answers would have contradicted the advice to the Minister contained in the 2011 Minute'.[86]

123. I have examined all the materials provided to me by the EISS Board and by SA Superannuants, as listed above. With the limited exception of the matter on which I comment in the next paragraph, I am satisfied that the responses have been reasonable, and have accurately reflected the true situation. I do not see any administrative error in the advice and responses outlined above.

124. The limited exception relates to the response dated 1 August 2007 sent to the Australian Services Union by the EISS Chairman. An attachment to this response does not fully answer a question about whether the EISS Board provided advice to the Treasurer concerning the making of the variations to the scheme rules in June 2002. The answer given is that a response should be sought from the Treasurer. Whilst this a correct statement, advice was provided to the Under-Treasurer on behalf of the EISS Board in the letter dated 7 June 2002, and in my view this should have been disclosed.

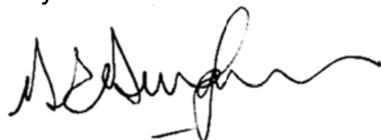
Opinion

I do not consider that since 2002 the department or the EISS Board has provided misleading advice in connection with the Treasurer's decision on the method used by EISS to calculate its taxed-source pensions.

Ombudsman comment

The amount of material provided to my investigation by the EISS Board, the department and SA Superannuants demonstrates that over the past 10 years there have been significant public resources spent on examining the concerns of SA Superannuants in relation to this issue. This has included a number of legal opinions obtained by the EISS Board, and by the department.

The subject matter of the parliamentary referral is of interest to SA Superannuants and the members of the EISS Scheme, because they consider that a change in the approach to administering the scheme would be of direct financial benefit to them; and because of what they see as a possible precedent for future changes to the broader state scheme. However, in my view the matter does not raise any issues of wider public interest.



Richard Bingham
SA OMBUDSMAN

30 June 2014

[86] Second SA Superannuants submission, p26.

Appendix A

SIGNIFICANT EVENTS SINCE 2004
Information provided by EISS Board

Early Feb 2005
A Retirement Seminar was held at Torrens Island Power Station (TIPS) by the Chief Executive Officer (EO) that resulted in lots of questions on the tax offset provisions.

March 2005
The EO held another meeting at TIPS to discuss the tax offset issue. The members' view of the perceived difference between the EC Act and the Rules was first raised here.

March/April 2005
The EO held further discussions with Mercer and members on the issues raised. Updates on the Scheme's review of the tax offset rules were provided in May and June.

June 2005 Corporate Governance Meeting
The Committee briefly discussed the issue based on a short history.

The Committee asked for:
- A review of the original decision
- A paper to the EISS Board showing examples of the benefit reduction outcomes that may apply to individual members

June 2005
FOI request received by RESI Corp from a Member of the Legislative Council on the advice given by Mercer on the effect on pensions of the conversion of Scheme to taxed status. This was passed to Treasury (as advice was given to Treasurer).

June 2005 EISS Board Meeting
The issue was raised at the EISS Board meeting after contact from TIPS members who were unhappy with progress to date. The EISS Board requested the EO to inform members of progress, which was done.

July 2005 EISS Board Meeting
A discussion paper prepared by the EO was tabled and discussed. This paper is attached as an example of the consideration that the Board gave this issue over a number of years, including seeking legal, actuarial and tax advice.

The recommendation in this paper was that:
- Benefits continue to be paid in accordance with the Rules
- Simple member communication be prepared
- Administration system be configured to allow for the offset.

The EISS Board were not able to accept this recommendation due to a possible discrepancy between the EC Act and the Rules that was raised at the meeting.

The EISS Board requested that:
- Legal advice be sought on the conflict between the EC Act and the Rules. If this advice was supportive of current practice, then the
- recommendation could be accepted.
- Draft communication to members be prepared

The legal advice was discussed at the August 2005 Board meeting.

August 2005
Further queries received from TIPS members

August 2005
Written advice on the EC Act vs. the Rules provided by DMAW. This advised that the EC Act and the Rules were consistent, provided that the net benefits under the Rules were no less than the net benefits under the EC Act.

Sept 2005
More questions from TIPS members, requesting a meeting.

Sept 2005 EISS Board Meeting
The EO was asked to:
- Summarise previous discussions and resolutions and circulate to the EISS Board.
- Get written advice from DMAW re EC Act vs. Rules
- Invite DMAW to the next Corporate Governance meeting
- Put the tax offset information sheet on hold

Oct 2005
The Chief Executive Officer held a meeting at TIPS on Monday 24 October 2005 with members to discuss the Contribution Tax Offset. The meeting discussed the history and structure of the Tax offset, particularly its effect on pension benefits. Members were concerned about perceived inequities in the Rules, and possible conflicts between the rules and the EC Act.

The members were previously unaware that the Treasurer made the Rules concerning the tax offset, and not the EISS Board. The advice the Scheme received from DMAW stated that the EC Act and the Rules were not in conflict. The members requested a copy of that advice. The EISS Board agreed to DMAW providing a one page summary.

The members were also informed that, to change the Scheme rules, the EISS Board would need clear evidence that a member was disadvantaged by the current rules at the time that a benefit was paid (or commenced to be paid) compared to the pre-privatisation situation. The Chief Executive Officer asked the members to put forward a letter to the EISS Board stating their concerns and how they feel they are being disadvantaged.

November 2005 EISS Board Meeting
A summary of the legal advice on the tax offset on pensions was provided to the EISS Board, who agreed to make it available to members. Advice distributed and posted on website. The EISS Board also requested that the appeal process under Clause 12 of the EC Act be formalised

December 2005
R Vear wrote to two EISS Board members expressing his concerns over the calculation of the tax offset. A response was provided to all the points in this letter on 16 January 2006.

Jan 2006 Corporate Governance Committee meeting
The Committee discussed a draft appeal process under clause 12 of EC Act. This process was never finalised, though this would not have prevented the hearing of any appeals under clause 12.

March 2006
A spreadsheet illustrating the calculation of the tax offset on pensions was released to members. This spreadsheet was available on the website, and individual data was loaded for members on request.

March 2006
A seminar on the tax offset was held at Keswick.

June/July 2006
The EISS Board discussed legal advice on the effect on the tax offset rules of the 2006 Federal Government Budget changes to superannuation.

DMAW provided advice to the EISS Board that the EC Act did not require net benefits to be maintained on the new rules after 1 July 2007, as the equivalence was based on the tax rules at privatisation. The EISS Board agreed to make a submission to Federal Treasury on the tax changes.

Jan/Feb 2007
This is also when the EISS Board was first approached by members wanting to take their pension on an untaxed basis, as allowed under Rule 31 of Division 1.

Advice was received in January 2007 from DMAW that Rule 29 and its application are valid under the EC Act, despite the fact that the reductions on individual member benefits are not matched against reductions in employer costs. This was in answer to concerns raised by members.

At the February 2007 meeting, the EISS Board resolved to provide a summary of the recent legal advice on the tax offset to members and employers.

The Board further resolved to voluntarily come under the jurisdiction of the Superannuation Complaints Tribunal, to provide members with an independent appeals process.

Mar 2007 Board meeting
The EISS Board resolved that the tax offset formula remain unchanged after 1 July 2007. This was based on previous legal advice that members would not be adversely affected, and that clause 5 of the Trust Deed required that employer liabilities not increase due to changes in taxation.

Apr 2007 Board meeting
The EISS Board resolved to stop payment of new untaxed pensions pending a favourable tax ruling, based on advice from DMAW. This was due to uncertainty about the provision of untaxed benefits under the 2007 tax laws.

June 2007
The EO and the Chairman met with members at Keswick to discuss the tax offset at length. The issue was extensively covered during this meeting. Over 100 members attended. Members requested that the EISS Board write to the Treasurer on their behalf.

August 2007
Detailed correspondence was sent to members as a consequence of this meeting.
The Scheme responded to Johnston Withers Lawyers letter of May 2007. Johnston Withers had been engaged by the ASU on behalf of disaffected members.

The scheme wrote to the Treasurer, as requested by members.

The Scheme wrote to employers re recent correspondence, and to ask if they would consider a change to the tax offset rules for pensions, to impose a cap on the reduction for pensions.

KPMG lodged an application on the Scheme’s behalf for a private ATO ruling on paying untaxed pensions.

The Scheme wrote to Division 3 members providing an update on the untaxed pensions tax ruling, the SCT and the letter to the Treasurer.

September 2007 Board meeting
DMAW provided advice on a discrepancy between the calculation of the tax offset on lump sums and the rules as inserted by the Treasurer. This discrepancy had only just been noted. Treasury confirmed that the intention was that the tax offset on lump sums would be no more than '15%.

The EISS Board resolved to seek a OC's opinion on whether the Scheme is acting in accordance with the EC Act in calculating the tax offset, both on lump sums (due to the discrepancy) and pensions.

The brief was delivered to Phillip McNamara QC in November, and his opinion received in December.

Dec 2007
Letter received from the Treasurer in answer to our letter of 2 August 2007 advising that Crown Law considers the tax offset rules are valid and in accordance with the EC Act.

Feb 2008 Board meeting
The EISS Board reviewed the QC's opinion.

DMAW advised the EISS Board that the opinion confirmed that
a. the Board's application of the pension tax offset was appropriate and may continue;
b. the Board did not have a basis for applying a 15% cap to the lump sum tax offset.

July 2008
The EISS Board resolved to amend the rules to fix the 15% limit on the lump sum tax offset after discussions with employers, and to write to members and employers.

Johnston Withers wrote to Chairman and EO with more queries arising from our letter to them of Aug 2007.

Aug 2008
Rule change limiting the lump sum tax offset to 15% accepted by all employers.

3 Nov 2008
The Chairman wrote to the ASU in response to a letter written to the ASU by Ray Hickman of the SA Superannuants (and forwarded to the EISS Board by the ASU). This response stated:
- Costs were determined on a scheme-wide basis, and the cost of a taxed pension may be less than an untaxed pension
- The EISS Board is required to comply with the rules, and cannot arbitrarily change them

Our understanding is that this letter was to be posted on the ASU website.

January 2009
The EO and DMAW met with ASU, APESMA and Johnston Withers to discuss the issue. This meeting was the subject of an article in a later ASU newsletter. We offered to review some case history calculations (from Mr year) that were discussed at the meeting, on the basis that we were given the assumptions underlying those calculations. These were not provided. We followed it up in July 2009 but no response was ever provided.

October 2012
Inquiry called for by Parliament.

The EISS Board also received a letter from the Superannuation Complaints Tribunal regarding a complaint from Mr Vear on the EISS Board's disclosure regarding the tax offset provisions.