



Australian Government

**Australian Government response to the House of
Representatives Standing Committee on Tax and Revenue
report:**

Tax disputes

DECEMBER 2015

BACKGROUND

On 2 June 2014, the Minister for Finance and Acting Assistant Treasurer, Senator the Hon Mathias Cormann, referred terms of reference for an inquiry to the House of Representatives Standing Committee on Tax and Revenue (the Committee). On 4 June 2014, the Committee adopted the inquiry, which was to inquire into and report on disputes between taxpayers and the Australian Taxation Office (ATO).

The Terms of Reference for the tax disputes inquiry called for the Committee to have particular regard to (i) collecting revenues due; (ii) fair treatment and respect of taxpayers; (iii) efficiency, effectiveness and transparency, from the perspective of both taxpayers and the ATO; and, (iv) how the ATO supports the outcomes of efficiency, effectiveness and transparency through the use and publication of performance information. The Committee was to examine these issues through a number of themes including small business, large business, high wealth individuals, and individuals generally. The Terms of Reference also noted that the Inspector-General of Taxation (IGT) may be available to undertake aspects of the inquiry if requested by the Committee.

On 11 June 2014, the Committee requested the IGT to undertake a review into the large business and high wealth individual (HWI) themes of the Inquiry. The IGT's report, *The Management of Tax Disputes*, was released by the Assistant Treasurer on 27 February 2015.

The IGT's report recommended (i) that the Government consider legislation to create a separate Appeals Group within the ATO, which would be headed by a new and dedicated Second Commissioner, responsible for managing tax disputes for all taxpayers; and (ii) establishing a framework for development of communications protocols between the Appeals Group and other areas of the ATO to ensure that the Appeals Group is, and is seen to be, independent in its dispute resolution function.

When releasing the IGT's report, the Assistant Treasurer noted that the Recommendation of the Inspector-General as well as those of the Tax and Revenue Committee would be considered by the Government on conclusion of its Inquiry.

The Committee tabled its report on 26 March 2015.

The Committee's recommendations can be divided into those for Government, which involve policy considerations and would normally require legislation, and those for the ATO, which do not involve policy considerations and can be implemented by the ATO as part of the Commissioner's administration of taxation legislation. Recommendation 2, however, includes both a recommendation for legislation and for changes to ATO administrative practices.

The Committee's report makes 15 recommendations specifically for the Australian Taxation Office (ATO) and five for the Government. The complete list of recommendations is at Attachment 1.

SUMMARY OF GOVERNMENT RESPONSE

The Government thanks the Committee for the work it has done in producing this report on an important issue.

The Government notes that the Commissioner of Taxation has statutory independence to administer, through the ATO, the principal Australian government taxation legislation. Consequently, how the ATO responds to its recommendations is a matter for the Commissioner of Taxation.

However, the Assistant Treasurer, after consulting with the ATO, recognised that the work of the Committee could be best advanced if the ATO's response is included as an attachment to the Government's response so that they can be read together. The ATO response is at Attachment 2.

The Government notes that, in general, many issues arising from the administration of taxation law may be addressed either by amending the law or by implementing administrative remedies such as improving guidance. For the Government, an administrative approach to the issues identified by the Committee has flexibility and timeliness advantages and does not multiply the volume of taxation legislation, which is difficult, time consuming and resource intensive to amend. An administrative approach, like legislation, is also subject to oversight and review, both via scrutiny agencies such as the Inspector-General of Taxation, the Auditor-General, the Administrative Appeals Tribunal (AAT), the courts, and also the scrutiny of Parliament and its committees.

The Government's detailed response to the Committee's recommendations to Government is set out below.

RESPONSE TO COMMITTEE RECOMMENDATIONS TO GOVERNMENT

Recommendation 2

The Committee recommends that the Government amend the tax laws and the Australian Taxation Office consider other administrative means by which interest charges would not act as leverage against a taxpayer during a tax dispute.

The Government partly supports Recommendation 2. It views a legislative response as excessive, embedding rules that would limit the flexibility of the Commissioner to remit interest charges after considering all the circumstances of each case. The power to remit the General Interest Charge in a manner that is fair and equitable to taxpayers currently lies with the Commissioner. Exercise of discretion subject to oversight enables a balance to be struck between the important function of interest charges in providing an incentive for taxpayer compliance and the requirement that taxpayers be treated fairly and sensitively during disputes. However, the issue has been raised and the ATO will work with Treasury to explore possible changes that could reassure the community about the fair application of interest charges.

Recommendation 7

The Committee recommends that the Government introduce legislation to place the burden of proof on the Australian Taxation Office in relation to allegations of fraud and evasion after a certain period has elapsed. The change should be harmonised with the record keeping requirements. These periods could be extended, subject to concerns of regulatory costs on business and individuals.

The Government does not support this recommendation. The Committee Report identifies a conflict between allocation of the burden of proof and the record-keeping requirements of tax legislation. In the absence of records, it may be difficult for a taxpayer to prove innocence from allegations of tax fraud or tax evasion. The Government understands that the Commissioner of Taxation is already committed to a range of administrative remedies to address this issue.

The question of whether 'fraud' or 'evasion' exists is already adequately dealt with in tax-related litigation, as may be seen from the relatively small number of reported cases on this question. In effect, the AAT

and Federal Court currently consider whether the ATO position on this question is sustainable on the evidence before them. Apart from review of such claims, a shift in the burden of proof to the ATO after a certain period has elapsed would be counter-productive and encourage sham behaviour by taxpayers associated with fraud and evasion. It would also unnecessarily complicate the tax-related litigation process and unduly confuse concurrent collection processes for cases involving potential 'fraud' or 'evasion'. The existing record-keeping requirements are operationally simple and align with the normal period of review for most taxpayers.

Recommendation 8

The Committee recommends that the Government introduce legislation to require judicial approval for the Commissioner of Taxation to issue a departure prohibition order.

The Government does not support this recommendation. A legislative approach requiring judicial review before Departure Prohibition Orders (DPOs) can be issued is not appropriate. The additional legislation would reduce the effectiveness of DPOs by reducing their timeliness. Adoption of this recommendation would also put tax administration out of step with agencies that make greater use of DPOs, such as the Department of Human Services. DPOs are not commonly used by the ATO, and are managed at a senior level and subject to regular review both within the ATO and by external scrutiny agencies.

Recommendation 11

The Committee recommends that the Government review the Small Taxation Claims Tribunal and determine whether it should continue. If so, there should be a one-off increase to the \$5,000 limit to take account of inflation since 1997 and a system introduced so the threshold increases incrementally in future to keep pace with inflation.

The Government notes that this recommendation has been overtaken by events with the passage of the *Tribunals Amalgamation Act 2015*, which provided for the Small Taxation Claims Tribunal to be subsumed within the Administrative Appeals Tribunal from 1 July 2015.

Recommendation 20

The Committee recommends that the Government establish a new position of Second Commissioner - Appeals, reporting to the Commissioner of Taxation to head up the new Appeals area within the Australian Taxation Office.

The Government does not support a legislative approach to the issue of separation of the taxation appeals area of the ATO from the compliance area of the ATO. The ATO has already effectively separated assessment and review by establishing a Review and Disputes Resolution area with responsibility for all objections, litigation, Independent Review, alternate dispute resolution and in-house facilitation that operates independently and reports directly to a Second Commissioner who is separate from the Compliance area that is headed by another Second Commissioner. As a consequence there is now no need for legislative separation.

ATTACHMENT 1 – Full list of recommendations by the Tax and Revenue Committee

Performance measurement and reporting

Recommendation 1

The Committee recommends that the Australian Taxation Office review its performance reporting measures and:

- develop a measureable key performance indicator of taxpayer perceptions of fairness in tax disputes;
- that this key performance indicator be monitored and reviewed by the Australian Taxation Office executive on a regular basis (at least half-yearly); and
- that the outcomes against such a key performance indicator be reported in the Australian Taxation Office Annual Report.

The legal framework

Recommendation 2

The Committee recommends that the Government amend the tax laws and the Australian Taxation Office consider other administrative means by which interest charges would not act as leverage against a taxpayer during a tax dispute.

Recommendation 3

The Committee recommends that the Australian Taxation Office amend its internal and external guidance so that it remits interest where:

- the Australian Taxation Office takes longer than the 60 days available to it to finalise an objection and the taxpayer has acted in good faith; and
- the Australian Taxation Office changes arguments after assessments have been made (such as during an objection or litigation).

Recommendation 4

The Committee recommends that the Australian Taxation Office amend its internal guidance so that findings or suspicion of fraud or evasion can only be made by an officer from the Senior Executive Service.

Recommendation 5

The Committee recommends that the Australian Taxation Office only make allegations of fraud against taxpayers when evidence of fraud clearly exists.

Recommendation 6

The Committee recommends the Australian Taxation Office should ensure that allegations of fraud or evasion are addressed as soon as practicable in an audit or review.

Recommendation 7

The Committee recommends that the Government introduce legislation to place the burden of proof on the Australian Taxation Office in relation to allegations of fraud and evasion after a certain period has elapsed. The change should be harmonised with the record keeping requirements. These periods could be extended, subject to concerns of regulatory costs on business and individuals.

Recommendation 8

The Committee recommends that the Government introduce legislation to require judicial approval for the Commissioner of Taxation to issue a departure prohibition order.

Recommendation 9

The Committee recommends the Australian Taxation Office better engage with taxpayers prior to litigation so that they are aware of what the model litigant rules require, and do not require, of the Australian Taxation Office.

Recommendation 10

The Committee recommends the Australian Taxation Office approach the Australian Government Solicitor to determine if they can provide advice and assistance to the Australian Taxation Office in terms of best practice in complying with the model litigant rules.

Recommendation 11

The Committee recommends that the Government review the Small Taxation Claims Tribunal and determine whether it should continue. If so, there should be a one-off increase to the \$5,000 limit to take account of inflation since 1997 and a system introduced so the threshold increases incrementally in future to keep pace with inflation.

Readiness to engage

Recommendation 12

The Committee recommends that the Australian Taxation Office implement recommendation 3.5.2 from the Inspector-General's report on alternative dispute resolution for all taxpayers (i.e. considering whether to engage in direct conferences with taxpayers at multiple points in a dispute).

Recommendation 13

The Committee recommends that the Australian Taxation Office give more consideration to taxpayers when making information requests, with priority given to:

- setting timeframes in practice statements, with a minimum of 28 days for all requests;
- giving taxpayers the opportunity to seek an extended timeframe upon receipt of a request; and
- giving reasons for an information request, typically based on a risk hypothesis.

Recommendation 14

The Committee recommends the Australian Taxation Office introduce a triage system for disputes so that, early in a dispute, matters can be escalated to ATO staff sufficiently senior or with the appropriate technical skills to resolve the dispute quickly and effectively. Such decisions should consider taxpayer fairness, among other criteria.

Other administrative matters

Recommendation 15

The Committee recommends that, as much as practicable, the Australian Taxation Office should give taxpayers written notice of issues and topics to be raised in section 264 interviews.

Recommendation 16

The Committee recommends that the Australian Taxation Office invite the Commonwealth Ombudsman to advise on improving its compensation processes, including compensation liability and amounts.

The governance framework

Recommendation 17

The Committee recommends that the Australian Taxation Office ensure that the information passed between an auditor and an objection officer surrounding a dispute only consist of the factual case documents, and the audit conclusion provided to the taxpayer. Any internal auditor commentary on the dispute should remain with the audit team.

Recommendation 18

The Committee recommends that the Australian Taxation Office develop protocols to ensure that an individual Tax Counsel Network officer only be allowed to provide advice or contribute to the provision of advice at the audit or objection stage of a dispute.

Recommendation 19

The Committee recommends that the Australian Taxation Office establish a separate Appeals area:

- under the leadership of a new Second Commissioner — Appeals to carry out the objection and litigation function for all cases;
- establish and publicly articulate clear protocols regarding communication between Appeal officers and compliance officers, including a general prohibition against ex parte communication, save where all parties are informed of, and consent to, such communication taking place; and
- empower the appeals function to independently assess and determine whether matters should be settled, litigated or otherwise resolved (for example, Alternative Dispute Resolution).

Recommendation 20

The Committee recommends that the Government establish a new position of Second Commissioner - Appeals, reporting to the Commissioner of Taxation to head up the new Appeals area within the Australian Taxation Office.

ATTACHMENT 2 – ATO RESPONSE TO TAX DISPUTE INQUIRY RECOMMENDATIONS

Recommendation 1

The Committee recommends that the Australian Taxation Office review its performance reporting measures and:

- Develop a measureable key performance indicator of taxpayer perceptions of fairness in tax disputes;
- That this key performance indicator be monitored and reviewed by the Australian Taxation Office executive on a regular basis (at least half-yearly); and
- That the outcomes against such a key performance indicator be reported in the Australian Taxation Office Annual Report.

A focus area of 'resolving disputes' has been included in the ATO's Corporate Plan 2015-19, as well as a new corporate key performance indicator from 2015-16 about disputes fairness.

In early 2015 the ATO commenced quarterly surveys of a sample of small business and individual taxpayers in dispute with the ATO, measuring perceptions of fairness in their dealings with the ATO. The survey results will inform the ATO's progress against the new corporate key performance indicator noted above.

Survey results indicate the importance of the effective and ongoing engagement with the taxpayer during the dispute process and ensuring the disputes process is independent and free from bias.

Recommendation 2

The Committee recommends that the Government amend the tax laws and the Australian Taxation Office consider other administrative means by which interest charges would not act as leverage against a taxpayer during a tax dispute.

Although this recommendation is a matter for Government, the ATO will work with Treasury to explore possible administrative and / or legislative changes that could reassure the community about the fair application of interest charges and to consider how our application of interest charges could be more in line with contemporary practices and community expectations. The ATO's agreement to recommendation 3 is evidence of our commitment to fairness and improved administration for taxpayers.

Recommendation 3

The Committee recommends that the Australian Taxation Office amend its internal and external guidance so that it remits interest where:

- The Australia Taxation Office takes longer than the 60 days available to it to finalise an objection and the taxpayer has acted in good faith; and
- The Australia Taxation Office changes arguments after assessments have been made (such as during an objection or litigation).

The ATO is currently considering this recommendation and is looking at how to best accommodate any required changes within its existing Law Administration Practice Statements and other guidelines.

Recommendation 4

The Committee recommends that the Australian Taxation Office amend its internal guidance so that findings or suspicion of fraud or evasion can only be made by an officer from the Senior Executive Service.

The ATO is currently reviewing its existing guidance material and working through how best to provide further clarity for its staff about the responsibilities and necessary considerations for an allegation or finding of fraud or evasion.

Recommendation 5

The Committee recommends that the Australian Taxation Office only make allegations of fraud against taxpayers when evidence of fraud clearly exists.

The ATO is currently reviewing its existing guidance material and working through how best to reinforce this message for staff and to better distinguish between the situation of making enquiries, as opposed to making allegations of fraud and / or evasion.

Recommendation 6

The Committee recommends the Australian Taxation Office should ensure that allegations of fraud or evasion are addressed as soon as practicable in an audit or review.

The ATO is currently reviewing its existing guidance material and working through how best to reinforce this message for staff and to better distinguish between the situation of making enquiries, as opposed to making allegations of fraud and / or evasion.

Recommendation 7

The Committee recommends that the Government introduce legislation to place the burden of proof on the Australian Taxation Office in relation to allegations of fraud and evasion after a certain period has elapsed. The change should be harmonised with the record keeping requirements. These periods could be extended, subject to concerns of regulatory costs on business and individuals.

While this is a matter for Government, the ATO is aware of the reach and nature of the fraud and evasion provisions and the perceptions this may generate for taxpayers if these provisions are viewed not to be used fairly. The ATO does not use these provisions lightly in its administration. The ATO will review its

processes and guidance material to reinforce for staff messages about not unfairly relying on the burden of proof and the absence of records beyond the required record-keeping periods.

Recommendation 8

The Committee recommends that the Government introduce legislation to require judicial approval for the Commissioner of Taxation to issue a departure prohibition order.

Contingent on the formal Government response to this recommendation, the ATO is not currently taking any action with respect to this recommendation.

Recommendation 9

The Committee recommends the Australian Taxation Office better engage with taxpayers prior to litigation so that they are aware of what the model litigant rules require, and do not require, of the Australian Taxation Office.

The ATO has commenced discussion with the Attorney-General's Department in relation to this specific recommendation.

Recommendation 10

The Committee recommends the Australian Taxation Office approach the Australian Government Solicitor to determine if they can provide advice and assistance to the Australian Taxation Office in terms of best practice in complying with the model litigant rules.

The ATO has commenced discussions with the Attorney-General's Department in relation to this specific recommendation.

Recommendation 11

The Committee recommends that the Government review the Small Taxation Claims Tribunal and determine whether it should continue. If so, there should be a one-off increase to the \$5,000 limit to take account of inflation since 1997 and a system introduced so the threshold increases incrementally in future to keep pace with inflation.

The *Tribunals Amalgamation Act 2015* which subsumes the Small Taxation Claims Tribunal into the Administrative Appeals Tribunal took effect on 1 July 2015. The ATO has updated correspondence issued to taxpayers to reflect this change.

Recommendation 12

The Committee recommends that the Australian Taxation Office implement recommendation 3.5.2 from the Inspector-General's report on alternative dispute resolution for all taxpayers (i.e. considering whether to engage in direct conferences with taxpayers at multiple points in a dispute).

Since July 2013 the ATO has introduced a number of initiatives and enhancements to the way it manages disputes, including:

- Encouraging early and direct contact with taxpayers or their advisors through the "pick up the phone" strategy.
- The continued and increased use of alternate dispute resolution (ADR) processes earlier in a dispute, using either external ADR practitioners (such as former judges) or independent ATO in-house facilitators, depending on the nature and scale of the dispute. In the 2014-15 year, 13 ADR processes with external practitioners were conducted (of which seven resolved the dispute) and 53 in-house facilitation processes were run (of which 35 fully resolved the dispute and five partially resolved the dispute). The ATO also participated in approximately 90 ADR processes initiated by the courts and tribunals.

Recommendation 13

The Committee recommends that the Australian Taxation Office give more consideration to taxpayers when making information request, with priority given to:

- Setting time frames in practice statements, with a minimum of 28 days for all requests;
- Giving taxpayers the opportunity to seek an extended time frame upon receipt of a request; and
- Giving reasons for an information request typically based on a risk hypothesis.

Contingent on any further direction being provided in the Government's response on this recommendation, the ATO is not currently taking any action with respect to this recommendation.

Recommendation 14

The Committee recommends the Australian Taxation Office introduce a triage system for disputes so that, early in a dispute, matters can be escalated to ATO staff sufficiently senior or with the appropriate technical skills to resolve the dispute quickly and effectively. Such decisions should consider taxpayer fairness, among other criteria.

Given that objections work has come together from a number of areas across the ATO into the Review and Dispute Resolution Business line as from 1 July 2015, work has commenced to understand and document all of the current processes for the management of disputes work. This work will progress to considering opportunities for streamlining, consolidating and improving in the way the ATO currently manages disputes- this will extend to include any triage system.

Work is also underway to reconsider the ATO's overall strategic approach to litigation management. Consideration is being given to how the right people can be brought onto the right case at the right time at all stages of a dispute.

Recommendation 15

The Committee recommends that, as much as practicable, the Australian Taxation Office should give taxpayers written notice of issues and topics to be raised in section 264 interviews.

Contingent on any further direction being provided in the Government's response on this recommendation, the ATO is not currently taking any action with respect to this recommendation.

Recommendation 16

The Committee recommends that the Australian Taxation Office invite the Commonwealth Ombudsman to advise on improving its compensation processes, including compensation liability and amounts.

The ATO notes that the scrutineer role for compensation matters has now transferred from the Ombudsman to the Inspector-General of Taxation (IGT).

The General Counsel area within the ATO has had meetings with the IGT to discuss our approach to compensation generally, and has been involved in a number of discussions about particular cases. The ATO will continue to discuss our approach with the IGT both generally and in the context of individual cases, as the relationship between the ATO and IGT develops.

Recommendation 17

The Committee recommends that the Australian Taxation Office ensure that the information passed between an auditor and an objection officer surrounding a dispute only consist of the factual case documents, and the audit conclusion provided to the taxpayer. Any internal auditor commentary on the dispute should remain with the audit team.

Communication Protocols governing the relationship between compliance officers, objection officers and taxpayers and a Service Commitment for Resolving Disputes have been produced. The ATO expects these protocols to evolve as a result of their application in the workplace and as practical examples arise for resolution. In putting together the Protocols and Service Commitment, external tax professionals were consulted.

Recommendation 18

The Committee recommends that the Australian Taxation Office develop protocols to ensure that an individual Tax Counsel Network officer only be allowed to provide advice or contribute to the provision of advice at the audit or objection stage of a dispute.

Communication Protocols governing the relationship between compliance officers, objection officers and taxpayers and a Service Commitment for Resolving Disputes have been produced. The ATO expects these protocols to evolve as a result of their application in the workplace and as practical examples arise for resolution. In putting together the Protocols and Service Commitment, external tax professionals were also consulted.

Tax Counsel Network officers will also be subject to these communication protocols. The protocols will ensure that a Tax Counsel Network officer involved in any way at the audit stage in a matter will not then be involved at the objection stage for the same matter.

Recommendation 19

The Committee recommends that the Australian Taxation Office establish a separate appeals area:

- **Under the leadership of a new Second Commissioner – appeals to carry out the objection and litigation function for all cases;**
- **Establish and publicly articulate the clear protocols regarding communication between the Appeal officers and compliance officers, including a general prohibition against ex parte communication, save where all parties are informed of, and consent to, such communication taking place; and**
- **Empower the appeals function to independently assess and determine whether matters should be settled, litigated or otherwise resolved (for example, Alternative Dispute Resolution).**

Effective from 1 July 2015, the Review and Dispute Resolution (RDR) business line within the ATO now has responsibility for all of the objection, independent review, alternate dispute resolution and litigation functions of the ATO. This satisfies the requirement for a separate and independent review area within the ATO, which is organisationally distinct from the ATO's compliance functions.

To strengthen independence and transparency of disputes decision making, comprehensive communication protocols and an overt service commitment now govern the engagement and ongoing relationship between RDR staff, ATO compliance officers and taxpayers. The communication protocols are based on principles of natural justice and transparency, ensuring in any dispute that taxpayers are informed as to the ATO's approach and information it holds upon which any decision is made. The protocols and service commitment were drafted following extensive external and internal consultation.

Recommendation 20

The Committee recommends that the Government establish a new position of Second Commissioner - Appeals, reporting to the Commissioner of Taxation to head up the new Appeals area within the Australian Taxation Office.

Contingent on the formal Government response to this recommendation, the ATO is not currently taking any action with respect to this recommendation.