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SUBMISSION TO JOINT COMMITTEE OF PUBLIC ACCOUNTS AND AUDIT

INQUIRY REVIEWING A RANGE OF TAXATION ISSUES WITHIN AUSTRALIA

INTRODUCTION

McKays Chartered Accountants was established in 1990 and has a broad range of business and individual clients. Our core business is the preparation and lodgement of Income Tax Returns. From 1997 we acted as Tax Agent for some taxpayers who had invested through a Financial Planner into various "mass marketed schemes" that were later denied by the Australian Taxation Office. We made a submission to the Senate Inquiry into Mass Marketed Schemes in 2001 and appeared at the hearings in Perth. Although this issue had a major impact on our practice and our impressions of the tax system in Australia this submission is not related to issues arising from the MMS debacle.

Our submission aims to deal with issues that mainly affect individual taxpayers, and small firms of Tax Agents, and is derived from systemic problems arising at the "coal face" on a daily basis.

PART A

The impact of the interaction between self-assessment and complex legislation and rulings.

- Product Rulings - The most important objective of our system of taxation should be certainty. Even with the current system of self-assessment a taxpayer should be entitled to certainty in their tax affairs. A clear example of this problem arises with Product Rulings for "tax effective" investments. At the time of entering into such investments, a taxpayer expects that all future deductions are "guaranteed" because it comes with an ATO Product Ruling. This it not so. There is an end date at which the Commissioner's Discretion to allow "non-commercial losses" to be claimed ceases. This is rarely made clear to the investor, or not understood. The onus is then on the Tax Agent to check the ongoing situation and look for extensions as they become available. On numerous occasions we have had to contact the project manager and argue the case with them, whilst also contacting the relevant department within the Tax Office to ascertain the true situation. A simple solution is available. A mandatory statement should be provided by the project manager annually, along with the income and expenditure for the year to 30 June, stating the Product Ruling number that is relevant to the project and when it expires. At present the Tax Return requires that the Product Ruling number be shown but does not require an expiry date to be stated.
- The numerous definitions of "income" are confusing, unnecessary, and increase the likelihood of error in completing tax returns. [Taxable income, Separate Net Income, Adjusted Taxable Income, income for the purposes of superannuation, payroll tax, Family Tax Benefits, other Centrelink benefits, CSA etc. etc.]
- We do not concur with the concept of pre-filled tax returns as we do not believe it can be done timeously. However, there are many items of income and expenditure that could be provided to the taxpayer in a way that greatly reduces the risk of omission, most of which is purely accidental. In a similar format to the annual statements supplied by Private Health Funds to members, advising of their days covered for Medicare Levy Surcharge purposes, there could and should be:
    1. Mandatory annual statements supplied to investors in listed companies recording dividends paid or credited to them. This would overcome the omission of dividends due to the belief that reinvested dividends are not assessable.
    2. Similar statements should be provided by banks and other financial institutions stating interest credited and debited to all accounts;

3. Medicare and Private Health funds should annually state the total amounts claimed and the gap (for Medical Expenses Offset). Generally, private health funds itemise all amounts claimed, whereas Medicare only states a total per person, which allows duplication or omission of some claims.
4. The State Revenue Office should annually report sales of motor vehicles (for GST purposes) and transfers of houses (for CGT purposes, showing the dates of purchase and sale) all of which would impress upon taxpayers the need to disclose taxable transactions.

In most cases we know that this information is supplied to the ATO, but at a much later date. With existing technology it should be possible to provide all this information to taxpayers by the end of July annually and thereby significantly reduce errors of omission.

- Tax Agent Portal and ATO website – the introduction of the portal has been widely lauded by Tax Agents and provides an invaluable source of information. In fact, being a Tax Agent would now be almost impossible without it. Both it and the ATO website are extremely beneficial and could be significantly improved. It is currently impossible to keep the portal open throughout the day. This means having to logon each time a new client is being worked on. It is also impossible to move forwards and backwards easily. The "search" facility usually results in "no results" and is virtually useless.
- Family Tax Benefits and interaction with Centrelink – Tax Agents have become welfare deliverers and at the same time have completely lost the ability to accurately estimate a taxpayer's refund or tax payable where there is a FTB component. The Centrelink report available on the Tax Agent Portal should be improved to provide a statement of the amount, if any, that has been paid to families in relation to FTB, so that an accurate tax estimate can be provided. Additional information regarding maintenance payments (through Child Support Agency) is also required as this further impacts on the FTB amount.
- Further in relation to Family Tax Benefits, there is a major issue of the high effective marginal rates of tax that apply at the thresholds. In particular, a low income taxpayer may have an effective marginal rate of 85% (on an income between $16,284 and $17,604).
- Child Care Tax Offset – yet another load of work and potential complication has been given to Tax Agents by the Tax Office. Clients are unwilling to pay for the time needed to access the relevant information from the portal. Clients who most need the benefit are the least able to pay increased fees. Most frequently the necessary Centrelink report has not been sent to the taxpayer and frequently taxpayers dispute the amount of their offset. In addition to this the government has marketed this benefit as not "means tested" however eligibility to it relies upon receipt of CCB (Child Care Benefit) which is means tested.
- Unified Capital Allowance System – the options now available for claiming (what used to be called) depreciation are now endless and confusing. Trying to explain Low Value Pools to a property investor or General Pools to a small business owner is almost impossible. All they want is a simple tax deduction for depreciation. The "Simplified Tax System" is the greatest misnomer ever invented.
- Personal Services Income – as members of an accountants' discussion group we regularly debate the correct way to deal with the increasing number of sub-contractors operating through a company or trust. In the vast majority of cases the existence of a separate entity is not through the intention of the taxpayer to minimise tax, but at the insistence of the "employer" in order to limit their employment obligations and provide a more flexible and less regulated workforce. The "80% rule" and the "results test" are not clearly understood and there is constant debate about compliance with the rules and their interaction with Part IVA. At present, the only way to determine the existence of a "Personal Services Business" with any certainty is to request a Private Binding Ruling. However, the main issue is that the ATO appears to believe that, even where there is a "Personal Services Business", the entity should distribute all net profit to the individual. [We cite the ATO document: "General Anti-Avoidance Rules and how they may apply to a personal services business."]

- Medicare Levy Surcharge – the imposition of an additional 1% tax on taxpayers without adequate hospital cover at taxable incomes over $50,000 (or $100,000 for a couple) is unreasonable, given that an income of this level is now well below that of a "high income" earner.

The application of common standards of practice by the ATO across Australia.

We make no submission in relation to this issue however, we do wish to note that, in general, our communication by telephone with the ATO has significantly improved in recent years. Although it can take 10 to 20 minutes (sometimes much longer) to finally get through to an ATO officer that can answer a question, or agree to further enquire into a tax matter, the general tone of that person and their apparent attitude to Tax Agents has changed for the better. It seems we are not (always) the enemy any more. However, the level of the ability of the "front line" tax officer to answer a question has significantly decreased to a frustrating point.

The level and application of penalties and the application and rate of the General Interest Charge and Shortfall Interest Charge.

- Whilst acknowledging the need to penalise those who underpay their tax, we concur with the majority to taxpayers and Tax Agents who believe that the GIC is an unfair imposition, being generally around 13% pa. compound. We submit that the interest rate itself should be in line with generally available rates from any other financial institution, and the addition of a non-deductible penalty is sufficient to penalise the recalcitrant under-payer, in line with their culpability.
- In many cases a taxpayer would willingly obtain finance from an independent finance house (bank or credit union etc) if the interest thereon were tax deductible. However, it remains an anomaly that GIC is tax deductible, when accrued, not paid, yet interest on borrowings to pay off a tax debt are not deductible. The removal of the deduction for GIC would be an alternative solution.
- From a regular review of our clients' ITA and ICA accounts we have formed the view that the accrual of GIC is a fairly random affair. There does not appear to be any consistent timing to the addition of GIC to an outstanding balance. The reporting of it to a taxpayer is also inconsistent. In many cases the existence of a debit balance on either account only becomes evident when a GIC notice is received.
- The report showing clients' balances shows numerous credit balances where we would not expect one; we believe that a taxpayer should be entitled to a regular (monthly or quarterly) statement showing all balances, whether credit or debit, to be sent directly to the taxpayer, not to us.

The operation and administration of the PAYG system.

- The PAYG system is very poorly understood by individual and business taxpayers; the abolition of provisional tax and its replacement by instalments has left many taxpayers unsure of their obligations. Frequently a June quarter instalment is unpaid by the time a taxpayer lodges their tax return; the ATO is inconsistent in applying a credit for this instalment to the assessment of an individual, thus it becomes impossible for a Tax Agent to accurately estimate tax payable or refundable.
- In particular, problems arise with annual PAYG instalments where the Tax Return is lodged prior to the payment of the instalment, due in October annually. The ATO will, generally, credit the assessment with the instalment, even though it hasn't been paid and isn't yet due. The taxpayer receives their assessment, which does not show that the instalment is still owing, and is, justifiably, confused when they then have to pay the instalment later. Taxpayers should be able to assume that, once their tax return has been assessed, that their tax obligations are complete for that year.
- The existence of the ITA (Income Tax Account) and a separate ICA (Integrated Client Account) balance creates extreme confusion and allows credits to sit on one account whilst a debit balance accrues interest on another. The tax payable by a taxpayer is simply one amount, and should be accounted for as such.
- The ATO should be asked to provide details of the numbers of taxpayers with debit balances owing, and the amount thereof, whether it be for Income Tax, PAYGI, PAYGW, GST or any other

tax type. We expect the number of debtors would be astronomical. There appears to be no consistent approach to recovery of outstanding debts. Some clients are terrorised into repayment arrangements that threaten to bankrupt them, whilst others (owing thousands of dollars) are left alone completely with no effort being made by either party to reduce the debt.

PART B

We make no submission on this.

CONCLUSION

We thank the Joint Committee of Public Accounts and Audit for the opportunity to make this submission and comment that there is no facility for taxpayers or Tax Agents to address systemic issues that arise on an ongoing basis.

Yours faithfully,

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