2 March 2006

Submission No: 32

To: The Joint Parliamentary Committee of Public Accounts and Audit

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We request that the name of the firm and individuals not be disclosed.

The Joint Parliamentary Committee of Public Accounts and Audit
Terms of reference: inquiry into taxation matters

We have summarised our key points in direct response to the individual terms of reference and also provided a detailed submission at the end that covers both part A and B

Summary

- **The self assessment system has created huge problems for honest taxpayers who have relied on expert advice and have had harsh penalties and interest imposed. Our example shows how a 236% penalty and interest can apply to a taxpayer who has followed expert legal advice and acted in good faith. This is a typical situation that a taxpayer can face under self assessment and is at the heart of the problem with the current system.**
- **The penalties and compounding interest have resulted in many taxpayers becoming insolvent, marriage breakdowns and, in the most extreme cases, the suicide of taxpayers. This is why there have been so many outcries over Mass Marketed Taxation Schemes and Employee Benefit Arrangements.**
- **The ATO seem to have a culture whereby they employ tactics not to take decent cases to court to resolve once and for all some issues**
- **The ATO force settlements on clients via the use of the penalty and interest system**
- **The system makes the assumption that all taxpayers are able to comply with self assessment and imposes severe penalties but the very complex nature of taxation laws mean that even the ATO can take years to form an opinion on certain legislation and change its opinion from time to time.**
- **The ATO do not always follow court judgements if they think they are wrong. We have provided a specific example of this.**
- **Any changes need to be made both retrospectively and prospectively as it is an ongoing problem that will continue to perpetuate unless taxpayers who have acted in good faith are treated fairly. Many of these disputes come about because the ATO retrospectively change their view or fail to act on a situation that has been occurring for years.**

- **Settlements are inconsistent and subjective and seem to favour very large taxpayers or large groups of taxpayers**
- **The ATO should automatically reduce interest and penalties for most taxpayers and then impose higher penalties for only the minority of taxpayers who do not act in good faith or have no arguable position**
- **The ATO should fund many more strong cases without the imposition of penalties and interest so that points of dispute are quickly resolved and all taxpayers can lodge their returns under the self assessment system with far more certainty**

Background:

We are a mid sized Chartered Accountancy Firm. In 1997 and 1998 a small number of our clients entered into what are now known as Employee Benefit Arrangements (EBA). This was done at the time under the direction of a partner who is no longer a partner of the firm. At the time these transactions were entered into we and our clients were advised that there were QC opinions and private rulings issued by the ATO that supported the making of such claims. Claims of this type had been made for a number of years by many taxpayers and were widely known about in the profession and the ATO. The claims were primarily made for the purposes of funding employee benefits or retirement and made in good faith under the self assessment system. These clients are the focus of many of our comments but the same issues are involved for any taxpayer in dispute with the ATO under the self assessment system.

Part A
the administration by the Australian Taxation Office (ATO) of the Income Tax Assessment Act 1936 and 1997 (including the amendments contained in the Tax Laws Amendment (Improvements to Self Assessment) Bill (No. 2) 2005) with particular reference to compliance and the rulings regime, including the following:

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

Key Points

- **The legislation and rulings are vastly more complex and voluminous now than they were at the time of the introduction of Self Assessment. The penalties and interest imposed are harsh and unfair to taxpayers who have acted in good faith and obtained expert advice.**
- **The ability of the ATO to issue an amended assessment with no burden of proof results in the ATO acting as both revenue collector and judge in many cases. It also allows them to be wise after the fact (sometimes years after). This coupled with the penalty and interest system has been a disaster for our clients.**

- The way the penalty system operates makes it very difficult for taxpayers to consider court action. In our real world example below the taxpayer faces a 236% penalty and interest bill if they decide to go to court and challenge the ATO or a 46% penalty and interest amount if they settle with the ATO. In addition the costs of a court action mean that on economic grounds most disputes do not go to court even when the taxpayer has a strong argument. This leaves other taxpayers without clear guidance under the self assessment system and the problem of disputes and grey areas perpetuates.
- The ATO should both fund and actively pursue court cases that will give clear guidance to all parties where an area of the law is uncertain. By selecting strong cases rather than the weakest both the Taxation Office and the taxpayers would benefit from a clear understanding of exactly how the laws operate in relation to certain arrangements. Once cases have been decided then and only then should settlements proceed with other taxpayers in the same situation if appropriate and not before. The interest and penalties however should not be imposed at rates that leave honest taxpayers who act in good faith in a disastrous financial position.
- When claims have been made in good faith and with appropriate advice the ATO should automatically exercise the discretion that they have available under the legislation to treat taxpayers in a fair way and significantly reduce interest and penalties (in many cases to nil) and not impose 40% + penalties and 12% + interest compounding daily. These reductions should not occur after years of dispute and as a mechanism to avoid court action or as a result of extensive criticism in Parliament or the press.
- By putting the entire burden on taxpayers to prove that their claims are valid under self assessment the ATO have developed a culture of not taking issues to the courts to get independent decisions. Rather they prefer to issue an enormous volume of complex rulings that are their interpretation of the law. Without issues being tested by the courts it may be years or decades of uncertainty that exist for taxpayers.
- The ATO is contemptuous of Court decisions and in some cases have publicly stated that they will not follow a decision and will take future cases to court. This is an abuse of the ATO's position and they like all other Australians should follow the law as determined in the courts. An example is that of Essenbourne's Case where it was held that FBT did not apply to a particular arrangement and the commissioner issued a statement that he did not agree with the findings and would be taking further cases to court. See Appendix 1. To date the other two cases that we are aware of have upheld the decision in Essenbourne and this decision stands some three years later as do the FBT assessments issued against our clients.
- Any changes should apply to both prospective and prior situations. The ROSA legislation in part addressed these issues but the prospective only nature of the legislation that was clearly designed to fix the systemic problems existing within the system leaves hundreds of thousands of taxpayers at the mercy of the ATO for many years to come. It seems that much of the change could be delivered by the ATO under existing legislation if the ATO altered

their internal policies and hard nosed attitude. It seems however that they cannot be relied upon to implement these measures internally without Government intervention and/or a legislative approach such as the ROSA legislation. We urge you to correct this situation.

- **The ROSA legislation 1/7/05 being prospective simply strengthened the ATO retrospective action of August 2002 when amended assessments were issued relating to prior 30/6/2000 transactions (when the legislation changed), i.e. Prospective 1/7/05 legislation sanctioned Retrospective ATO actions 30/6/00 having the effect of being retrospective. To this day MPs and Senators take the ATO required position.**
- **The retrospective change of view by the ATO in the case of EBA's and other issues has left many taxpayers in situations of extreme financial hardship. There have been bankruptcies, marriage breakdowns and suicides with, we predict, more to come over issues that are subsequently being "settled" by the ATO in some cases (not all cases) with much lower interest and penalties but many years too late for many taxpayers.**

the application of common standards of practice by the ATO across Australia;

Key points

- **The ATO seems to be settling these matters in completely inconsistent and unfair ways.**

- **There are three rates of penalty being used in concessional settlement offers by the ATO 10%, 5% and 0% in the case of EBA's alone. The final penalty that is imposed is based on a judgement by the ATO that is in many cases a subjective decision.**

- **There are four rates of daily compounding interest being applied: Full GIC (currently 12.63%), 6.28%, 4.72% and 0% for different periods in the case of EBA's. Once again it seems to be a subjective decision that benefits some taxpayers over others. We enclose the recent speech of Mr Don Randall, Liberal, Canning WA. See the highlighted sections re settlement and who we are dealing with.**

- **It seems that the more tax involved or the larger the number of taxpayers the better the deal that you get. It was widely reported in the press that the Reserve Board member Mr Gerard paid only 50% of the primary tax due and no interest and penalties to settle a dispute that one of his Companies had with the ATO. The amount in dispute of course was much much larger than any claimed by our EBA clients who on average have claimed deductions between $200,000 and $300,000 over a two year period.**

- **Clients who are not part of a widely based dispute have almost no hope of getting a reduction in the interest and penalties as they do not have the leverage to force the ATO into a reasonable position.**

They are left in an impossible financial position and may face penalties and interest of 200% plus as shown in our example.

- **It seems that in these circumstances and with so many people involved the ATO should err on the safe side and give the fairest possible deal to everyone even if a few people get the deal who do not deserve to get the deal. It seems that the assumption that most taxpayers are out to cheat the system and so the penalties are harsh so as to act as a deterrent is extremely unfair. The reality is that it is only a very small minority who act in a bad way but the majority get caught up in severe penalties and interest designed to catch the minority. The alternative of reviewing every taxpayer is hugely costly for both the ATO and the individual taxpayers as they are required to make extensive submissions and provide supporting documentation. There is still a presumption of guilt rather than innocence and it is the ATO acting in a judicial capacity to see if they meet their criteria for remission. Our experience of reviews of individual circumstances leaves a lot to be desired in what is a costly and subjective exercise and should not be the basis for reductions in penalties and interest. We understand that if you do not agree with the decision that the ATO has formed your only recourse is to undertake Federal Court action as the Administrative Appeals Tribunal is not able to review such administrative decisions. The Federal Court is a much more expensive and risky proposition as you can have costs awarded against you.**

- **It would also seem that if a reduction in the interest and penalties is possible then this should also be available to those taxpayers who wish to take the matter to the courts and any final resolution for all taxpayers should await the final outcome of cases that fully examine the arrangements. The situation where the ATO take an obviously weak case to court and then hold that up as a definitive decision should also be stopped. There are examples in the area of EBA's where some of the cases involved people who had just entered some journal entries and of course these taxpayers were held not to have made deductible contributions to an EBA. Cases where people made the contributions to the EBA for a reasonable sum and used those funds for the correct purpose have not been before the courts.**

- **In the Mass Marketed Tax Schemes there was a case heard before the courts that the ATO won and then a settlement offer was made on the basis of no interest and no penalties and two years to pay the tax. We have made a number of submissions to the ATO to explain why some of our clients who invested in those products received such a settlement and asked why the clients who invested in the EBA's are being treated so differently. The Inspector General of Taxation's Report examined this in detail and he found that the same factors that were used to determine the granting of the concessional treatment applied in both the Mass Marketed Schemes and EBA's in many cases.**

the level and application of penalties, and the application and rate of the General Interest Charge and Shortfall Interest Charge; and

Key Points

- **As outlined in the first and second parts of our submission to responses to the enquiry the application of the interest and penalties is placing an enormous burden on taxpayers. The rates imposed on our clients result in interest and penalties greater than 200%.**
- **The impact of daily compounding interest at 12%+ over protracted disputes results in an equivalent simple interest rate of 20%+ over a seven year period.**
- **The Taxation Commissioner has announced that he would cap the interest and penalties to 70% in the case of EBA's only but even this represents an enormous penalty in a situation where in the main taxpayers acted in good faith and relied on expert advice. It seems that the interest and penalty are designed to penalise people who either deliberately ignore commonly accepted practice or try and use the Commonwealth as a source of finance. People who are involved in disputes were often made aware of the ATO's view up to four years after the return was lodged. The process of issuing amended assessments can then take another several years and if the person objects against the assessment this can take another couple of years for the ATO to make a decision. This means that it is extremely likely that the dispute will not be resolved for at least five to seven years after the original deduction. As our example shows this leads to huge penalty and interest bills that taxpayers cannot jump over.**

- *the operation and administration of the Pay As You Go (PAYG) system.*

We have not made a submission at this stage

Part B
The Committee shall examine the application of the fringe benefit tax regime, including any "double taxation" consequences arising from the intersection of fringe benefits tax and family tax benefits. "

Key Points

While we have not commented on family tax benefits the use of FBT in the case of EBA taxpayers has resulted in multiple assessments being issued for both Income Tax and FBT. While the ATO have stated that they will not enforce both assessments they also have not removed the FBT assessments. This leaves the taxpayers with a huge debt position that puts enormous strain on the taxpayer and pressures them to settle disputes. This is even more frustrating when considering our comments in relation to the cases that have held that FBT is not applicable in our client's circumstances (see appendix 1).

Regarding suffering financial hardship with multiple assessments, during the last five years or so it has been impossible to approach banks and raise finance and keep up commitments. To suggest taxpayers send "evidence of inability to secure borrowings" is naive. The lending authorities re bank overdraft etc. would only have needed one sniff of the magnitude of the amended assessments and liquidation or foreclosure would have been instant. The massive strain of signing financial accounts each year and non-disclosure of both huge ATO multiple assessments and ACIS requirements have caused stress and worry. All this time taxpayers did not see themselves as having done anything wrong.

Detailed Submission – relates to parts A and B

The impact of self assessment has been a devastating blow to those clients who made claims in good faith and then face enormous fines and compound interest when disputed by the ATO. We have outlined below a general example that gives you a common position for taxpayers where penalties and interest have amounted to 236% of the original tax in dispute. This is not an exceptional position and accurately reflects the position of many taxpayers facing a prolonged dispute with the ATO. This 236% figure ignores doubling up of assessments (the practice of issuing multiple assessments to different taxpayers for the same tax liability) and the imposition of Fringe Benefits Tax that is discussed in part B of the submission. We have clients who face total tax liabilities with interest and penalties of more than 10 times the original tax in dispute. This put enormous pressure on those clients to settle the matters with the ATO.

It seems that in the case of EBA's the ATO had a change of view towards these claims in 1999 when they placed an embargo on the issue of further private rulings and when they realised the extent of the claims. We understand that prior to this date they had issued approximately 60 private rulings on EBA's. The penalties and rates of interest are extremely harsh when applied to their full extent. The ATO have the discretionary powers to reduce the interest and penalties in these cases but have declined to do so until the matters are now starting to appear before the Administrative Appeals Tribunal (AAT) and Federal Court some seven years after the original deduction was claimed.

We and our clients have cooperated fully in the provision of information to the ATO and feel that we are being blackmailed into settling the disputes when faced with enormous interest and penalties being imposed. Not only do taxpayers face the huge legal costs that are associated with a court case but also the reality that if they settle with the ATO they could end up paying a fraction of the penalties and interest than disputing the tax. In our example below the penalties and interest are reduced from 236% to 46% and in most of the mass marketed tax schemes of course the penalties and interest were reduced to nil. These circumstances force taxpayers to settle. Consider the following example

Example
If a company claimed a deduction for $300,000 in 1997 then the "tax saved" would have been $108,000 (36%).

If this claim is then later disputed by the ATO, even though the client had legal advice and there are no court judgements to date that reflect the facts of this clients case, they would face penalties and interest to date of 236% of the primary tax. Our calculations and assumptions are set out below.

If the dispute had dragged on and the original amended assessments were issued in 2003 and objections were lodged in say 2003 and only now decided by the ATO then the client would currently be facing a total debt some seven years later of approximately $362,000. If that client were to settle with the ATO they may be able to negotiate a 5% penalty and 4.72% interest over the period. The total payable under this settlement would be $158,000. This illustrates the impossible position in which taxpayers are being placed. If the taxpayer decides to take the ATO to court they are faced with arguing a total debt of $362,000 + legal costs and the potential to have to pay the ATO's legal costs. If the taxpayer lost they could face $700,000 + in tax, penalties, interest and costs (including the ATO's costs). If they settle today they would have to pay approximately $158,000.

We make reference to an article in the Australian Newspaper by Sir Harry Gibbs and attach a copy for your information. The article outlines the complexity that results in even the most learned legal minds being unable to fully comprehend the Act. When legal experts or Judges cannot agree as to interpretation how can most taxation advisors who are generalists or let alone an ordinary taxpayer have any hope of full comprehension.

It must be noted that we are talking about situations where there are solid opinions (from expert solicitors and QC's) as to the correctness of making a claim and not just a speculative claim in the hope that the item is deductible. It seems that it is this speculative claim or outright deception that should invite such harsh penalties. The EBA claims were made in an environment where private rulings had been issued to individuals accepting EBA arrangements and no general ATO advice existed. Of course if the guidance provided by the ATO is itself complex and not clear as to provide definitive guidelines or as in many cases provides a general exclusion to Part IVA (the general anti avoidance provisions) then those rulings provide little assistance to accountants or their clients. There was a time when the ATO would issue a ruling after the outcome of a case that in many instances they had funded to determine the exact operation of the law. **It is a running joke in the accountancy profession that when the ATO win a court case the decision applies to every taxpayer across the board in its widest interpretation and a general legal principal is created. But when they lose a case the decision only applies to taxpayers with the exact same circumstance and facts of the case and a narrow interpretation is taken by the ATO.** (See press cutting)

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Please put yourself in our clients' position.

They are small business owners who on the whole have been unable to make significant superannuation contributions over the years to fund their retirement

as they have had to in many cases keep the funds in the business as it has grown. They are hardly sophisticated taxation experts. They have been advised of a way to make a significant catchup contribution to an EBA that will make them much more secure in their retirement. They were advised that this had been done now for a number of years by other taxpayers (in some cases going back to the early 1990's) and was undertaken by the large accounting firms and the extremely wealthy. They were advised that there were QC opinions and positive private rulings from the ATO that supported the deductibility of the claim. They were advised that there were thousands of other people going into this type of arrangement. They decided to put in a lump sum figure and claim a deduction. Imagine now their horror in the way that they have been treated by the ATO. They have been treated like tax cheats, had penalties and interest of 236% imposed and advised that if they do not settle they will face legal costs in the hundreds of thousands of dollars. On the other hand if they settle they will pay interest and penalties of 46% and they can get on with their lives.

What would you do in these circumstances; is this the way the ATO should behave?

We would have thought that the ATO would take into consideration the part it played in creating this confusion and uncertainty and the good faith that the taxpayers had when they entered into the arrangements. The ATO should say to the taxpayers: We will fund several decent test cases on these issues. If taxpayers win the case well that's the end of these issues for taxpayers. If the ATO win the cases then no interest and no penalties should be imposed and the taxpayers should have a decent period of time say two years to pay the tax.

Foot Note: From our small press samples

So much for what we read in the press from time to time and the numerous answers from our appeal to Government members and Senators. As at today, every one of our clients are all holding, after seven years, both FBT and duplicated IT assessments (some multiple taxpayers as well) 40% penalties and 12.62% cumulative interest to date. No politician who recently voted for ROSA 1/7/05 (instead of 1/7/00) knows what he or she has done financially to many SMEs by supporting the retrospective pre 30/6/00 action of the ATO. How can any taxpayer negotiate a settlement that is fair with this duress hanging over his or her head as at today?

ATTACHMENT 1

Extract from ATO website 23 February 2006

Essenbourne

On 17 December 2002, the Federal Court handed down its judgment, in which it considered the deductibility of 'contributions' purported to have been paid under an employee incentive trust. The Court held that an income tax deduction was not allowable for an amount contributed by a company to an employee incentive trust because the payment was simply a distribution of the company's profits to the three principals of the company.

However, the Court disagreed with the Tax Office's view that fringe benefits tax (FBT) should apply.

In relation to FBT, we are of the view that the Court's decision is not correct and inconsistent with our understanding of the intent of the FBT law. However, we consider that the Essenbourne case is inappropriate for clarifying the FBT law on an appeal to the Full Federal Court given her Honour's finding that the contribution to the employee incentive trust was a profit sharing exercise of the three principals of the company.

Further Extract form ATO website 23 February 2006

In the related Spotlight Stores decision, the Court held that the contribution to the incentive trust did not amount to the provision of a taxable fringe benefit. The Court concluded that it should follow its earlier decisions in Essenbourne and Walstern because they were not clearly wrong.

ATTACHMENT 2

Transcript of Mr Don Randall's Speech (early December 2005)

TRANSCRIPTS OF SPEECHES:

A. Don Randall – Liberal, Canning WA

"Mr RANDALL (Canning) (1.33 p.m.)—I am pleased to speak on the Tax Laws Amendment (Improvements to Self Assessment) Bill (No. 2) 2005. At the outset, I say that I totally concur with the member for Hunter's sentiments on the bill itself, rather than with some of the subsequent comments. I very much concur with the fact that he has identified that many of the people caught up in these arrangements were of an honest, hardworking nature but were led into arrangements by people who made a lot of money themselves and who now seem somewhat absolved of the malaise they have cast over the people induced into the arrangements. However, the people who went into the arrangements believed they were doing so legally and, as a result, have been caught and absolutely smashed by the Australian Taxation Office. I will be referring to this issue later in my speech.

The ROSA bill, as it is commonly called—review of self-assessment—is a bill that is very much needed because of the maladministration of the tax office under Mr Carmody. The ROSA bill was perpetuated by the people the member for Hunter referred to—people who believed they had sound advice from financial agents and national accounting companies and who eventually involved themselves in what they believed was a proper function of tax minimisation. For those who do not think that tax minimisation is legitimate, let me just point out that everybody is entitled to try to reduce the amount of tax they pay as long as it is legal. If these people thought they were doing something legal, good luck to them—if it was legal, good luck to them—but do not change the rules on them on the way through so that they did something they believed was legal on the best possible advice but were subsequently absolutely crucified.

Even before my election as the member for Canning, I was approached by people caught up in arrangements and schemes for assistance in their fight against the

Australian Taxation Office. Since I have been the member, I have been fighting this issue, as many of my colleagues will know—and the Australian Labor Party seems to know now—and I have no shame in being a signatory to Senator Johnston's letter to the Treasurer asking for a fairer deal for people who were caught up. A significant number of coalition members and senators share the same sentiment, and I thank them for their support in this fight. The fact is that the seat of Canning had been held by the Labor Party for 15 of the previous 18 years, and I think that the constituents wanted somebody who would get their hands dirty and get stuck into the issues they were facing. We are the people who represent the connection between huge bureaucracies funded by the government, like the Australian Taxation Office, and them. If they cannot get help, where do they go? If the tax office will not help them, it is people like us, as representatives of this House, who are obliged to give whatever assistance we can. That is our job.

One of the big issues affecting the constituents, not only in my electorate but in Western Australia generally and elsewhere, has been the ATO's practice of changing its position on taxation matters and the retrospectivity in applying that changed view to taxpayers who mistakenly thought the ATO could be relied on. As I said, this is one of Mr Carmody's sad legacies. His legacy will be the punitive use of his office against the mum and dad businesspeople of Australia. Everybody thinks he was great in collecting a record amount of money, but anyone could have done that, given the current climate. His legacy will be that he has persecuted a lot of small taxpayers.

I recognise that the way this matter was handled could have had a major impact on the election result in areas of Western Australia. For example, the member for Kalgoorlie invited the Prime Minister to his electorate to visit victims of the mass-marketed tax investment schemes disaster. As a result of visiting the Kalgoorlie electorate, the Prime Minister initiated measures to introduce the office of the Inspector-General of Taxation as a taxpayer advocate and an independent adviser to the minister on systemic problems within the ATO.

Sadly, in a recent meeting with the Inspector-General of Taxation I received first-hand confirmation that the commissioner had largely ignored the recommendations and agreements made after the IGT inquiry into the consistency of the commissioner's actions in these disputes. In fact, it appears that the Inspector-General of Taxation had been stood over by the Commissioner of Taxation, Mr Carmody, and quietened. I know that those at senior levels of government have also spoken to the IGT about his speaking out publicly when he appeared to be in conflict with the Commissioner of Taxation. I find it quite disturbing that he should be stood over in such a manner. As the IGT was unable to resolve the matter, it became even more important that, as elected representatives, we continued our efforts to bring this matter to a conclusion.

The impact of the ATO altering its position is much more serious than just a massive tax bill. In most of the cases, the retrospective application of the commissioner's change in view affects arrangements that these taxpayers have made for their retirement and superannuation or their ability to continue in business. The impact has been so significant that in many cases the taxpayers have committed suicide, lost their family home or lost their business. I saw this first-hand the other day, and there are people meeting in this House today whose husbands have committed suicide as a result of these assessments. I have therefore done my best to help the constituents see their way through this very personal trauma. Very early in the piece I recognised that at the centre of these disputes there was clear evidence that the ATO accepted these arrangements and in fact gave numerous advices and opinions

confirming the validity of the arrangements, as self-assessment allows.

It was only when these arrangements became popular and, in the ATO's view, adversely impacted on revenue, that the ATO decided to change its position. This is something I do not understand: either the tax law allows these arrangements or it does not. It is not the Commissioner of Taxation's duty to decide what is or is not allowable because of revenue considerations. That is the duty of the legislators of this parliament to do that. Perhaps that is why we should be bringing these measures back to the parliament, so that we can have a say, rather than the Commissioner of Taxation going off on his own jaunt.

One of the categories of these arrangements that the ATO originally classified as mass marketed but subsequently excluded so as to avoid the settlement recommended by the Senate inquiry into mass marketed arrangements is employee benefit arrangements. In these cases, the ATO issued over 60 favourable opinions, only to alter this position years after they had acted. It is also important to recognise that the Commissioner of Taxation administers the tax law by administrative practice—that is, if every taxpayer sought a private binding ruling on every transaction or arrangement, the commissioner would be overwhelmed and unable to respond and do his job. Consequently, most matters are dealt with by broad rulings or practices in the form of verbal advice or general acceptance over periods of time by the ATO. In many cases, taxpayers do not have any option but to follow the administrative practice. As the use of an administrative practice is for the convenience of the Commissioner of Taxation and not the taxpayer, it is even more reprehensible for the commissioner to change position and then inflict the cost of the change on the taxpayer. Because of that, for the last five years, along with many of my colleagues, I have maintained an absolute determination to rectify this great injustice that has been perpetrated on Australian taxpayers.

The tax dispute over employee benefit arrangements has occupied an enormous amount of the time and energy of members of this House, trying to get the ATO to see sense and acknowledge its own substantial contribution to this debacle. During that time, the Taxation Office has maintained its belligerent view that taxpayers with employee benefit arrangements were nothing other than tax cheats—as the member for Hunter has outlined—and deserved the treatment they were receiving. That treatment included being issued with three assessments for the one deduction—a neat trick that the commissioner justifies by stating that his office does not know which assessment is correct and therefore all possibilities must be covered. This approach by the commissioner begs the question: if the commissioner does not know then how is the taxpayer expected to know?

As I said earlier, although originally included as a mass marketed arrangement, the commissioner subsequently excluded employee benefit arrangements from the mass marketed settlement and continued to impose penalties of 40 to 50 per cent, with interest at a rate of 13.72 per cent. Because of this approach, taxpayers could not pay or settle with the ATO, the dispute continued and the sorry saga was never settled. Every time taxpayers tried to ask the Taxation Office which bill they should pay, the commissioner said that he did not know—'Just sign this blank piece of paper and when you have signed it I will think about it and tell you which one.' What sort of accountability is that? Who would sign a blank piece of paper saying that you will pay whatever bill he comes up with?

I am very pleased to announce today, thanks to the intervention of the Assistant Treasurer, Mal Brough, that there has been a breakthrough for EBA taxpayers. The

Assistant Treasurer is a hard man with a job that he has to do—that is, to support the collection of revenue in this country and see that there is no risk to revenue. But, unlike previous assistant treasurers and the Treasurer himself, Mal Brough, the Assistant Treasurer, decided he would actually get his hands dirty and meet individual constituents on this issue. And he is doing it today. As we speak, he is in his office meeting more individual taxpayers who are suffering this absolute trauma that the Taxation Office has dragged them through. I have only credit and admiration for him in that he has not hidden behind words and said: 'We can't influence the Australian Taxation Office. It is an independent statutory body. There is no way in the world that we should involve ourselves in this'—absolving themselves in such a Pontius Pilate fashion so that they do not have to do their job. Mal Brough is doing his job, not only his statutory job—

The DEPUTY SPEAKER (Mr Hatton)—I remind the member for Canning that he should refer to the member as the member for Longman.

Mr RANDALL—The member for Longman is also doing the right thing by people that have suffered the persecution of the Australian tax office. I commend and congratulate him, and I wish that the previous speakers had done the same.

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Although I am unable to go into specific detail, it appears that all EBA taxpayers will be able to settle their disputes by paying one taxing point instead of three. In the last few weeks, the tax office finally announced the new arrangement that there will only be one taxing point, not two or three as imposed by the assessments. Instead of there being 40- to 50-per-cent penalties, it will be a five-per-cent penalty. Instead of being more than 13 per cent, the general interest charge will be 4.72 per cent for the entire period across the board. That is a huge breakthrough, which could and should have been done years ago. Now people can finally settle.

It has always been my view that these taxpayers should not have paid any penalties or interest. However, in the interests of resolving this impasse and dispute, it seems that this is a reasonable compromise to bring to an end a very sorry episode in our tax administration. I would add, however, that had the ATO been prepared to make these concessions several years ago, when the position was first changed, the interest that is now payable would not have accrued. It has been the commissioner's steadfast refusal to discuss the matter or act reasonably that has imposed these additional interest costs upon these taxpayers.

I commend the Tax Laws Amendment (Improvements to Self Assessment) Bill (No. 2) 2005, as I said at the beginning, which in the future will prevent the commissioner from imposing a penalty or interest when an administrative practice is altered—but more on that later. As I said, I support this bill, but it does not help the people that helped generate this bill—the people that were caught up by these arrangements before; it is helping people prospectively. In the immediate future, I trust that the minister will allow me to continue to work to assist him in convincing the new management of the ATO to bring outstanding mass marketing disputes, as well as retirement village and securities lending arrangements, to a close in a similar manner.

In many ways, pushing this issue towards a fair and equitable conclusion has placed me in a position of conflict with many of my colleagues, but that has not been my aim; it is just a product of the fight. When examined closely, the issues are not all

that complicated. The seemingly endless stream of whitewash and self-justification put out by the ATO has cloaked this dispute in so much legalese that few MPs could get to the core of it, and that has probably contributed to the differences of opinion. After all, surely we should be able to rely on the considered views of the ATO. However, as far as these disputes are concerned, my experience is that we cannot, and that is a problem that I am going to continue to pursue with vigour.

I mentioned earlier that I had more to say about the ATO's practice of reversing bad decisions and then blaming everyone but itself. After reviewing the self-assessment system, Treasury recommended that when the ATO alters an administrative practice it should only be applied prospectively. I do not believe that anybody would argue that that is not a fair and equitable approach by an administrative office. In accepting Treasury's recommendations in full, the Treasurer—on behalf of the Howard government, Treasury and the ATO—acknowledged that the fair and reasonable approach is to apply these changes prospectively. However, for the last five years that is exactly what the ATO has refused to do. Is it only fair and equitable in the future but not in the past?

I am not slow in taking our public administration to task when it gets it wrong. The ATO in particular has almost unlimited legal and technical resources, and because of that we should require that it accepts the financial consequences of getting it wrong, not use discretionary powers to transfer those consequences to taxpayers.

The second of the ROSA bills goes part way down that track, although it still needs to be amended to fully implement recommendation 6 of the Treasury's review of self-assessment. Without this, the bill will perpetuate the problem we have struggled with for five years or so and in some ways, because it hands the commissioner even more discretionary power, spark new disputes, and the cycle will continue. I urge the government to raise the bar of expectation on the tax administration to stand by its advice and wear the cost of error, as every other entity and individual in this country is required to do. Amending this bill will start that process, so that is something I would like to see.

We live in a world of shifting values, but it is our duty in public office to be consistent. Fairness and equity should not be an option for either government or is instrumentalities. When it is sidestepped to protect incompetence, government is obliged to step in.

Finally, I feel compelled to comment about what I see as a common misconception among commentators about the leadership at the ATO. We have experienced a dramatic shift in the size of revenue over the past several years. Repeated budget surpluses have been applied wisely to reduce our public debt and insure our economy against future difficulties, and tax receipts are at an all-time high.

This growth in revenue is the result of the policies of the Howard government and its management of the economy. Company tax revenues are high and still accelerating because the government has developed the economic climate to encourage that. Our health and wealth are the results of good government by elected representatives and not a result attributable to the efforts of the tax commissioner. Frankly, a drover's dog could have collected the revenue under the same conditions, and I suspect that an administration in which taxpayers had confidence that advice was reliable would have collected even more and without disputes in an atmosphere of conflict.

I look forward with expectation to a new management at the ATO that is responsive to the concerns of members of parliament instead of dismissive of them. However, I

am not that encouraged by the fact that there is a new taxation commissioner coming in the form of Mr D'Ascenzo. I have met with Mr D'Ascenzo in the past, along with Mr Marizza, Mr Fitzpatrick and Mr Konza. Interestingly, at a recent meeting with D'Ascenzo and Konza, I found D'Ascenzo most patronising and dismissive. At this particular meeting, besides me, the members for O'Connor, Indi, Mackellar and Wentworth—a whole lot of members—were discussing it with him, and he had the temerity to say that we as elected representatives did not seem to understand and know what we were talking about.

If that is the way he is going to start his administration of the Australian Taxation Office—putting down the federal members as not knowing or understanding what they are talking about and placing himself on an intellectual plane above us on these matters—I do not have a great deal of faith in his direction. I am told that Mr D'Ascenzo has never worked anywhere but the Australian Taxation Office. As a result, I do not know that he has ever really got his hands dirty or has any wide experience in any other area. If he continues as a sneering apologist for Mr Carmody's style of leadership and administration, I have grave doubts that the Taxation Office will go forward under that sort of administration.

I will give Mr D'Ascenzo the benefit of the doubt and see if he can be his own leader in the Australian Taxation Office rather than following sheep—following Mr Carmody's lead. That can only be bad for Australian taxpayers given the maladministration that Mr Carmody presided over. The fact that he collected record amounts of money does not mean to say that he administered the Australian tax office well. He was just a man picking up the tab.

I recommend the ROSA bill. It is addressing a need in terms of the maladministration of the Australian Taxation Office. I will be watching its implementation and, as an elected representative, making sure that the Australian Taxation Office does its job, that it does not persecute honest, hardworking taxpayers of this country and that we get the best possible administration out of the office."

ATTACHMENT 3

THE AUSTRALIAN

Print this page

Clean-up for tax law 'disgrace'

David Uren and Steve Lewis
26jan05

THE Howard Government has secret plans to use its Senate majority to dramatically simplify onerous tax laws, including stripping back the 7000-page tax act.

In a reform push that will be welcomed by business, Treasury has been quietly developing a plan that reverses the present approach to dealing with tax avoiders.

The plan will see the tax act set out broad principles rather than take the existing approach, which makes the law so detailed that it closes every loophole.

The current laws were described by former High Court chief justice Harry Gibbs yesterday as a "disgrace".

Treasury and the tax office will then be called on to issue regulations and rulings to show how the new tax laws will work in practice.

Dick Warburton, chairman of the Government's tax advisory board, said tax simplification had been discussed for years.

"If we're ever going to achieve anything, it has to be within the next 12 months. We've got to get something going now or it will be shelved," said Mr Warburton, who is chairman of oil giant Caltex and a former Reserve Bank director.

Referring to the majority that the Government will enjoy in the Senate from July, Mr Warburton said: "We've got a better chance now of getting it through with the current political process, although there shouldn't be huge controversial change."

He said the new approach would be tested with some new legislation, expected to cover tax arrangements for large companies, to be released within the next few months.

"But it won't be tested without a lot of consultation first."

Sir Harry lent his weight to the call for reform, saying much of the legislation was "obscure to the point of being incomprehensible".

"The legislation is already voluminous compared with our own earlier legislation and with other tax systems, and the volume increases from year to year," Sir Harry says in an article in The Australian today.

He said the law gave excessive power to the tax office, and was an overreaction to the decisions by the High Court under Garfield Barwick in the 1970s.

ROSA pre 1/7/05 makes it far worse

However, he warned that reforming the act could not be left to Treasury and the tax office.

The push to streamline the raft of tax laws comes as Peter Costello yesterday warned a group of Coalition MPs pushing for big tax cuts that their ambitious plans had to be fully paid for.

"If anyone wants to put ideas to the Government on tax they are very welcome to do so," the Treasurer said.

"But the ideas obviously have to be consistent with keeping a balanced budget, keeping low interest rates, properly funding the health system, social welfare, our defence commitments (and) the war on terror, because we aren't going to give any of those things up."

The ginger group of Coalition MPs wants the Government to use its Senate majority after July 1 to push through big tax reform, but has come under pressure from Finance Minister Nick Minchin to detail how these big spending plans will be funded.

However, other government ministers have supported the tax reform push, with parliamentary secretary Chris Pyne claiming there is an "overwhelming view" among Liberal MPs for lower taxes.

Family and Community Services Minister Kay Patterson encouraged the ginger group to continue its work.

But the lack of consultation in developing the new approach has been criticised by tax specialists.

"The whole development of a principles approach has been done under a veil of secrecy," Taxation Institute tax director Michael Dirkis said.

"The fact that it was not the subject of consultation is illustrative of how easily consultation can be avoided when a government or administration is so minded," he said.

Mr Dirkis said there were risks in relying on broad principles and leaving the rest to regulation. The number of regulations could mushroom, and they were not subject to the same level of scrutiny as new legislation.

Tax lawyer Mark Leibler, who is included in this year's Australia Day honours list, said he favoured a return to legislation that set out basic principles rather than inordinate specifics.

However, he added, consultation on such an overhaul should be broad, meaningful and "not done secretively".

Assistant Treasurer Mal Brough, who is driving the project for the Government, disputed there has been a lack of consultation.

THE AUSTRALIAN

Print this page

Harry Gibbs: The chance to clarify tax law

26jan05

EVEN viewed in the light of the momentous happenings of the year, it must surely be agreed by supporters of all political parties that the recent federal election and its results were of considerable significance to all Australians. The fact that the Government will have control of the Senate as well as the House of Representatives is both an opportunity and a temptation.

The Government now has an opportunity to ensure the passage of necessary legislation which the Senate had previously prevented, sometimes on grounds of mere caprice. On the other hand, unfettered power tempts holders of that power to abuse it by, for example, enacting legislation that unduly favours one section of society or is otherwise oppressive or unfair in its operation. It is, of course, hoped that the Government will seize the opportunity and resist the temptation.

There are many matters that obviously appear to call for reform in the interests of the nation and which will no doubt require the attention of the Government. Many of these matters will give rise to controversy – for instance, the reform of industrial relations is likely to attract the opposition of the unions, and the achievement of a commonwealth-state plan to ensure the continued flow of water in our inland rivers will probably cause some states to hold back because of the financial consequences.

There is, however, one reform which, if successfully implemented, should (in Macbeth's words) buy "golden opinions from all sorts of people", even one hopes from the officials of the Treasury and the Australian Taxation Office.

This reform may at first sight seem insignificant compared with other matters of great moment that will be considered by the Government, but in fact would be of very great benefit to business, trade and the community generally.

The reform to which I refer is the rewriting of the income tax legislation. This does not necessarily involve issues concerning levels of taxation. The laws relating to income tax are a disgrace. There is nothing new in that reproach – it has been true for at least a decade, the only change being that the situation is getting worse.

The legislation is absurdly voluminous compared with our own earlier legislation and with other tax systems, and the volume increases rapidly from year to year.

Much of the legislation is obscure to the point of being incomprehensible. It gives the Australian Taxation Office unacceptably wide discretionary powers, including those given by the anti-avoidance provisions of part IV(a), which were inserted in an overreaction to some earlier decisions of the High Court.

It is, I think, true to say that many practising accountants no longer try to unravel the mysteries of the legislation by reading its provisions. Rather they rely on the various documents and rulings issued by the Australian Taxation Office – a subordination of the rule of law to the opinions of the Executive. The uncertainty of the law is an impediment to business generally.

What is needed is a completely new statute of manageable size and clearly drafted. By clarity of drafting, I do not suggest that there should be a repetition of the ill-fated attempt to put the income tax law into "plain English". Without clarity of thought, there can be no clarity of expression. If the present obscurities of the law were removed, there would be no need to confer on the Taxation Office discretionary powers that are offensively wide.

Such a task, if undertaken, could not be left to the Treasury and the Australian Taxation Office, although officials from those bodies might of course provide invaluable assistance. The undertaking should be carried out under the supervision of a body including representatives of business, the legal and accountancy professions and academe, and if thought necessary, experts from the US and the UK. It would not be an easy task, but its successful completion would be a lasting achievement to the credit of the Government and something of lasting value for Australians generally.

I have said that this proposal would not necessarily entail any considerations of taxation levels. One would hope that the taxation scales will be reviewed. However, that review should be a separate exercise from the rewriting of the legislation and should be kept separate from it because, whereas there are likely to be widely differing views as to what scales are appropriate, there should be general agreement that the tax law should be rendered clear and accessible.

The rewriting of the taxation law could provide simplicity; the achievement of equity is another question.

Harry Gibbs, former chief justice of the High Court of Australia, is president of the Samuel Griffith Society. This is an edited extract from his Australia Day message to its members.

www.samuelgriffith.org.au

ATTACHMENT 4

AUSTRALIAN FINANCIAL REVIEW 19/11/2004 3+

Taxman relents on staff schemes

Fiona Buffini and Lenore Taylor

KEY POINTS

- The crackdown on staff benefit tax schemes has involved 7000 taxpayers.
- Some 20 government MPs have taken the taxpayer's side in the dispute.

The Tax Office has backed down from its hardline position on employee benefit tax schemes, offering to cut interest penalties by two thirds after a highly-critical report by the Inspector General of Taxation.

The Howard government is hoping the settlement will end a long and bitter dispute with up to 20 of its own MPs who have been campaigning for years on behalf of the 7000 taxpayers who found themselves with often large tax debts when the Tax Office cracked down on the schemes that proliferated in the 1990s.

While the courts have consistently struck down the schemes as tax avoidance, the Tax Office has agreed to substantially reduce interest charges as the crippling interest debts were holding up resolution of the issue, which involves $1.9 billion in tax deductions.

But the offer falls short of backbenchers' demands for no interest or penalty charges and they claim the inspector general's recommendations were watered down.

The Tax Office will write to taxpayers offering to reduce the general interest rate used to calculate penalties from 12.44 per cent to 4.7 per cent and cap interest accrued before January 2005 at 70 per cent of the primary tax.

As a result, interest will average 30 per cent of the primary tax instead of up to 90 per cent and multiple assessments will be cancelled. The schemes involved channelling income through staff benefit trusts.

Inspector General David Vos said his first review proved it was important for the Tax Office to consider taxpayers' individual circumstances in contentious cases.

"When you do a broad-brush treatment of a wide range of taxpayers the last thing you should be doing is be aggressive," Mr Voss said.

"This will lead to a fairer outcome, with reduced interest and penalty payable by many. Importantly, the Tax Office has agreed to review and publish new guidelines for the future."

Assistant Treasurer Mal Brough said while the courts have repeatedly ruled against the schemes, it was important all taxpayers "who have been drawn into these situations are treated fairly".

But West Australian backbencher Don Randall said he was not sure the problem had been solved.

"It's a disgrace it's taken so long to arrive at any decision, the jury is out on whether it really relieves the tax burden that these people are under and I am sceptical about a Tax Office panel doing the assessing because of the Tax Office history in this matter."

Tax Institute tax director Michael Dirkis said: "This represents a resolution of the last vestige of the mass-marketed schemes from the late '90s. It's a common-sense solution."

ATTACHMENT 5

AUSTRALIAN FINANCIAL REVIEW 3
FRIDAY 11/3/05

ATO's test cases to be scrutinised

Allesandra Fabro

KEY POINTS

- There are concerns the Tax Office adopts a 'win at any cost' approach.
- Lawyers say the ATO is 'tardy' in paying the bills of cases it is funding.
- The way court and tribunal decisions are applied will be reviewed.

The way the Australian Taxation Office selects and funds test cases will come under scrutiny over the next few months, as the tax watchdog launches a review into tax litigation practices.

The Inspector-General of Taxation, David Vos, will review the ATO's so-called test case program and its approach to general litigation.

"Taxpayers and their advisers tell me that the Tax Office does not always act appropriately in cases being litigated with taxpayers," Mr Vos said yesterday.

"The Commissioner of Taxation has at his disposal resources to fight a case which are not available to the average taxpayer. There are concerns that, as a result of these resources, the Tax Office adopts a 'win at any cost' approach to litigation."

Under the test case program, the ATO can elect to fund certain cases that could have a determinative effect on the way tax law is interpreted.

But the program has often been seen as controversial, particularly in such areas as mass-marketed schemes where the applications for test case funding of a number of taxpayers were rejected, leading to accusations that the ATO was "picking winners" or selecting those cases it thought it had the best chance of winning.

There have also been complaints – usually from lawyers – that the ATO is tardy in paying the bills of those cases it has agreed to fund.

The federal government, following the recommendations of the Treasury Review of Self Assessment, asked the Inspector-General to conduct the test case program review.

The Inspector-General has expanded the scope of the review to include all aspects of litigation, including the way the ATO applies court and tribunal decisions.

Some tax advisers suggest that decisions are only selectively applied, and that the ATO draws on favourable decisions as being "broadly applicable" across most taxpaying groups, while those that are unfavourable to the ATO are held to be "fact specific" to the individual case.

"Clarification of tax law is an important aim of tax litigation," Mr Vos said.

"However, taxpayers must be satisfied that the Tax Office in administering tax litigation is not abusing its position and that it is not acting in breach of its obligations to be a model litigant.

"In our review, we will be examining the concerns of taxpayers and their representatives on these matters and the extent to which they are valid."

Submissions to the review close on April 29.