SUBMISSION
ON

Review of Aspects of Income Tax Self Assessment

BY

RESOLUTION GROUP AUSTRALIA

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1 Introduction

Resolution Group Australia (RGA) represents and assists taxpayers and their accounting and legal representatives in dealing with tax disputes.

RGA are not accountants, lawyers or tax agents. Consequently, RGA does not give taxation, financial or legal advice. All of the tax disputes have arisen as a result of the taxpayers own actions or as a result of following advice from the Australian Taxation Office (ATO) or the advice of their financial, accounting or legal advisor.

RGA has focused on finding solutions for the dispute in a manner that protects both the rights of the individual and the revenue in dispute.

From about 1998 the ATO introduced global campaigns to disallow deductions and raise amended assessments against investors in mass marketed investment arrangements, employment benefit arrangements, equity linked bonds, retirement villages marketed under the umbrella of Taxation Ruling TR 94/24 and a number of other arrangements.

A common feature of each of these campaigns is retrospective application of a change in the ATO position and failure to individually examine each investor. In each case the ATO absolved itself of any responsibility for error or lack of certainty in the past and insisted that under the self-assessment system it was the taxpayers responsibility to know the law and how the ATO might interpret the law in the future. Each of these cases has shown that the taxpayers followed ATO advice including written advance opinions, private binding rulings and public rulings. Despite this level of "certainty" and administrative practice from the ATO, the taxpayers bear the full onus of proof to overturn amendments.

One aspect that has become clear is that the ATO itself is uncertain about how the law applies. In the case of employment benefit arrangements the ATO issued rulings that have subsequently been shown to misinterpret the legislation. The ATO while admitting that only one taxing point is appropriate have issued multiple amendments under Company Income Tax legislation, Fringe Benefits legislation and personal income tax legislation. These amendments are for the same transaction and amount because the ATO even after allegedly close examination could not decide which taxing point is correct.

The above raises two possibilities, the first is that the tax legislation is too complex and difficult for anyone including the ATO to interpret and apply with certainty. The second is that the ATO is incompetent and is not accountable for failing to administer the legislation correctly. Either possibility leaves the taxpayer in a dangerous position under self-assessment and this danger has crystallised for a large number of taxpayers thus leading to this review.

Self-assessment is dangerous because it tempts taxpayers to push the boundaries of the tax legislation. On the surface self-assessment appears harmless but the repercussions of mistakes or intentional wrongdoing are hidden and severe. The self-assessment system has generally failed so far because taxpayers have not been adequately educated, guided or protected from the disadvantages and dangers of the system. The ATO on the other hand has been over-protected. The most positive outcome from this review would be a restoration of the balance of responsibilities between the taxpayer and the ATO.

For the self assessment system to have credibility, it must truly be a self assessment system not the current pretence. Taxpayers should be able to self amend and increase their liability without incurring penalties and interest. Currently, self amendments increasing a liability incur an automatic application of 5% penalty plus full GIC. Entities that discover genuine errors must choose between self amendment and payment of these additional taxes or taking the risk that the error will not be discovered by the ATO. Many millions in revenue are lost because entities cannot pay the additional tax so they take the risk and generally are never discovered. The ATO should be focused on the collection of primary tax. Penalties and GIC must be the tools used to ensure future compliance. These tools must be used properly and fairly; if that is done compliance will improve. The ATO currently misuses these tools. They are used as a means of punishment, intimidation, inducement to settle on unfair terms and extortion. More taxpayers are being alienated and made les compliant as a result. Declaration of an amnesty could generate a significant amount of such revenue.

The ATO must be accountable for failures in administration, the ATO must take responsibility for its actions or failures to take action and the onus of proof must not rest solely on the taxpayer.

2 Response to Key Issues of Review- The Level of Reliance Taxpayers Should Be Able To Place On Tax Office Advice

2.1 Is Tax Office advice sufficiently accessible?

No. Although the ATO website has improved access to information, the website is slow and difficult to use. Information is hidden and requires expertise to find and understand. The Tax Pack is similarly unwieldy and difficult to follow. Access to ATO staff for direct advice is almost impossible. In addition advice varies from office to office and from person to person. ATO internal systems are fragmented so that many staff do not have a full picture of the structures and processes consequently their advice is inadequate or flawed.

The ATO must be made responsible for providing systems that educate and inform taxpayers of their rights and responsibilities. Until the ATO achieves its own responsibility taxpayers should not have to bear the consequences of any mistakes.

2.2 Should Tax Office advice indicate whether Part IVA applies to a particular arrangement as a matter of course, or only on request?

The ATO must state whether Part IVA applies to any arrangement as a matter of course. To leave it open is to only issue partial advice. The Commissioner is exercising his discretion under Part IVA at every opportunity. Consequently, it now forms part of his standard approach to administering the legislation and must therefore be stated, "not indicated" as a matter of course.

2.3 Are there significant problems with the accuracy of Tax Office advice? If so, how should they be addressed?

Yes, there are significant problems with the accuracy of the ATO advice and the escape clauses that the ATO attaches to its advice. The first issue that should be addressed is the escape clause attached to Private Binding Rulings where the ATO are only bound to honour their advice to the applicant. In a commercial world any advice soon becomes public and if the advice is correct then every other taxpayer in identical circumstances should be affected in the same way. There is a legitimate expectation that the PBR is correct therefore every other taxpayer should also be able to rely upon the ruling. If the ATO is incorrect then the ATO not innocent taxpayers must bear the responsibility. The current situation allows the ATO to escape the responsibility of its own wrongdoing.

The ATO system for providing advice must be improved so that the same advice issues from every office and staff training must be improved.

In essence any advice from the ATO must be binding to the extent that the ATO can only make prospective changes. Faced with this duty and responsibility the ATO will be encouraged to use its vast resources more responsibly.

2.4 Is there evidence of pro-revenue bias in Tax Office advice? What measures would improve confidence in the objectivity of Tax Office advice? Would an independent evaluation assist?

Yes, there is evidence of pro-revenue bias in tax office advice. As the collector of the revenue it is understandable that where the ATO is uncertain they will opt to protect the revenue rather than give advice that allows revenue to be lost. While that is a reasonable approach, in recent times the ATO has become aggressively protective and is actively seeking to find ways to collect more revenue rather than taking an objective approach to only collecting what is properly due.
As a result of the mass marketed arrangements the ATO introduced the system of product rulings. None of the rulings that have issued however, allow the use of non-recourse loans or geared investments even though in every case that has gone before the Courts, including Lau and Cooke, the gearing aspect by itself is not the disqualifying or non-complying factor. It is apparent from these product rulings that the ATO is disregarding the law and only issuing rulings that protect the revenue.

In Harris v FCT concerning Controlling Interest Superannuation the legislation was found to be ambiguous. The ATO had previously issued advice and PBRs favouring the taxpayer. However, as a result of the ATOs more aggressive approach, the ATO reversed its previous decision in favour of revenue collection. An independent process and evaluation will assist. There should be a separate body responsible for issuing rulings. This should be an independent panel appointed from legal and accounting professionals and at least one community representative, with sufficient power to actually be of value. The ATO and taxpayers should be able to make submissions but should not have any involvement in the appointment or funding of this panel. Rulings issued by the panel should be binding on taxpayers and the ATO. The panel must resolve any disagreement on interpretation of a ruling, application of particular circumstances or alleged non-compliance.

Improved communications between tax professionals and the ATO would also assist. That means more accessibility to ATO staff. The ATO staff must be trained to understand that they have a duty to act fairly and responsibly. The ATO must have a clearly defined and enforceable duty to act in accordance with the Taxpayer's Charter, to fully explain decisions, to reply without intimidation and in a timely manner.

2.5 How should Tax Office advice be framed to assist taxpayers — by explaining contending views of the law, or by setting out how the Tax Office intends to apply it? Does this impact on the way that advice is expressed?

Any objective analysis of a particular situation will consider and state the contending views before making a decision on how the matter will proceed. Consequently, the ATO advice must give both the contending views of the law and how it intends to apply the law. There must however, be an independent process available where a taxpayer disagrees with the way in which the ATO intends to apply the law and there is sufficient support for an alternative view.

If the ATO is to do its duty objectively then there should not be any impact on the way that advice is expressed.

2.6 How might the Tax Office clarify the circumstances in which general advice can be relied upon?

The ATO can clarify the circumstances by greater emphasis on taxpayer education and information. All taxpayer information documents could specify that where a taxpayer's circumstances are different that taxpayer might wish to contact a helpline that is readily available and has staff that can answer the query. If the information is readily and easily available then taxpayers have less reason for not knowing. Access to information by telephone or email that is answered quickly and efficiently and is reliable will be an improvement on the current situation.

2.7 Is there value in making more Tax Office advice legally binding? What additional safeguards would be required?

Yes, there is value in making ALL Tax Office advice legally binding. Advice in a context of penalties for mistakes, that is not binding or reliable is neither "advice" nor does it have value.

The safeguard is that the advice must be correct. The advice must clearly identify the circumstances and any variations and the effect of such variations. Correct and precise advice cannot be exploited. Even if the revenue is adversely affected by correct advice, it still means that taxpayers are obtaining what is rightfully theirs under existing legislation. Legislation must be simplified.

2.8 Should taxpayers be penalised merely for not following PBRs when self assessing their income tax liabilities?

No, mere failure to follow a PBR to the letter should not result in non-compliance or penalties. Variations that result from commercial necessity or unavoidable circumstances must be treated as complying. Penalties should only apply where there is deliberate non-compliance, artificiality or dishonesty.

2.9 If no penalty applied, would direct appeals against PBRs still be required?

Yes, on the presumption that the appeal is against the issue or refusal to issue a favourable PBR. The penalty process applies to non-compliance with a PBR after it has been issued and accepted by the taxpayer. If the taxpayer is dissatisfied with the PBR at the time of issue then the appeal or independent evaluation process must still be available.

2.10 Should the Tax Office be able to charge for PBR's?

No, provided that PBRs are made available to all taxpayers, then every application serves to clarify different tax outcomes in different circumstances. The ATO practice of issuing PBRs that were kept secret and used by promoters to market a particular product caused the growth of tax avoidance schemes.

Where a taxpayer pays for a PBR they may be entitled to keep the PBR private, as many have done in the past. This does not contribute to the growth of knowledge and understanding.

2.11 How could the Tax Office use more cost effective channels for the delivery of binding advice to taxpayers or through practitioners?

Email and the ATO website. Emails to the ATO must be able to be allocated a query number or other identifying feature. The ATO must respond within a stated timeframe and the response must be binding on the ATO.

3 Response to Key Issues of the Review - The proper time frame for amending assessments

3.1 Should the period for an amendment increasing the liability of an individual not in business, and/or a very small business be reduced to, say, two years? Should the eligibility of a very small business be based on whether it has chosen to be a Simplified Tax System taxpayer? What exclusions from a two year period would be appropriate?

Yes, the period for amendment increasing or decreasing a liability should be reduced to two years effective retrospectively. There should not be any eligibility criteria as this only introduces another layer to an already complex area.

Exclusions must include deliberate fraudulent activity. However, there must be a requirement on the ATO to provide evidence of the fraudulent activity before an amendment can be raised. In the current situation the ATO generally only assert fraud or evasion and raise amendments on the assertion. In many cases the assertion is not supported by verifiable evidence.

Even amendments for fraud or evasion should have a time limit. It is clear that the maximum time for retention of records is seven years and even the ATO destroys records after a time period. In those circumstances it is pointless having time to make amends but no supporting information.

3.2 Should the amendment period for medium and large businesses and other complex cases remain as four years?

No, the period should be standardised at two years. The less variations there are the less confusion there will be.

3.3 Should the amendment period for arrangements conferring unintended tax benefits (including arrangements covered by Part IVA) be reduced from six years to, say, four years? Should taxpayers be required to disclose certain tax planning arrangements more fully in returns?

No, the time period for any amendment should be standardised at two years. Part IVA can only apply if the tax deduction is allowable or if the income is not assessable. In other words the arrangement complies with the letter of the legislation. Part IVA has been greatly misunderstood and applied. Whatever was originally intended the practical consequences as confirmed by the Federal Court

is that Part IVA can only reverse what is in compliance with the legislation. It is therefore arguable that a disallowance of an otherwise allowable deduction is a lesser offence than a taxpayer claiming a deduction that was never allowable. Where an arrangement complies with the letter of the legislation if the Commissioner wishes to exercise his discretion to disallow the otherwise allowable deduction or assess the otherwise not assessable income, then the Commissioner must do so within a reasonable time frame. If anything the time period should be less, because these taxpayers have in fact complied with the legislation and the time taken to amend will result in additional GIC.
By way of example the ATO provides tax employees with the opportunity to "salary sacrifice". The ATO has a specific document outlining the benefits of salary sacrifice and the sole and dominant purpose is the tax benefit. Because the sole purpose of salary sacrifice arrangements are the tax benefit these arrangements fall within the scope of Part IVA and may be disallowed.

Taxpayers who purchase a rental property for the sole purpose of negative gearing and without any prospect of ever deriving a profit also fall within the scope of Part IVA and the Commissioner may disallow deductions from such arrangements. The mere scope for application of Part IVA should not mean that the time for amendment should be any longer than for any other amendment. Yes, taxpayers should be required to provide full disclosure. However where such disclosure is made the penalties should not apply.

4 Response to Key Issues of the Review - the appropriateness of the length of tax audits

4.1 Is there benefit in the idea of the Tax Office providing early notice to those taxpayers that it has decided to audit? What would be a suitable notification period? What exclusions from the notification regime would be appropriate? Would this idea still be beneficial if taxpayers had to disclose more information?

Yes, on the assumption that early notification means immediate action by the ATO in proceeding with the audit. There should also be provision for taxpayers to make an immediate, without prejudice, payment of primary tax and so avoid penalties and GIC. This will encourage taxpayers to co-operate and manage the effects of any adjustment.

In cases involving fraud or criminal activity then it not be appropriate to give prior warning, as it is likely that evidence may be lost.

4.2 Should a taxpayer who lodges a nil liability return be subject to the same time limits as apply in amending an assessment?

Yes, the legal escape hatches that the Commissioner continues to exploit must be closed. Where a taxpayer lodges a return under self-assessment that taxpayer believes that an assessment has been made. The discovery later that a nil assessment has been found by the courts not to be an assessment makes the term self-assessment a nonsense and again establishes a double standard against the taxpayer.

5 Response to Key Issues of the Review - whether taxpayers are adequately protected from unreasonable delays in enforcing the tax law

5.1 Should taxpayers have a remedy where the Tax Office delays unreasonably in issuing an amended assessment after it has all the relevant information?

Yes. The ATO should be liable to pay compensation equal to the penalties and GIC imposed by the legislation. This will act as a disincentive to the ATO to delay.

5.2 Should the period for an amendment reducing a taxpayer's liability be the same as for increasing liability, or be set at a fixed period?

The time period should be the same.

5.3 Would it be better to implement some of the possible changes raised in this Chapter (for example, early notification of compliance activity) by changing administrative procedures, rather than by changes to the law?

The ATO has established that it has difficulty understanding and complying with the law. It most certainly ignores administrative practices and these are more difficult to enforce. The law must be changed and there must be an independent process to enforce ATO compliance.

5.4 What (if any) clarification of the terms 'reasonable care' and 'reasonably arguable position' is needed?

It is not simply a case of clarification. The ATO must be obliged to show reasons why the taxpayer did not take reasonable care or why the taxpayer does not have a reasonably arguable position. In Prebble vs FCT the Court found that the taxpayer had a reasonably arguable position. Numerous written representations

had been made to the ATO that there was a reasonably arguable position, but the ATO ignored all these representations.
While clarification is necessary, there must be a process of independent review that does not involve the expense and time of taking the matter through the Courts.

5.5 What further guidance on grounds for remission of penalties is required?

There must be a requirement on the ATO to justify the imposition of penalties. The current system of remission allows the ATO to avoid responsibility for their contribution to the problem. The global campaigns have shown that the ATO remission policies involve a rote application of policy. This is a breach of administrative law and the taxpayer's charter. Individual consideration of remission decisions must be required.

5.6 What is the effect of the penalty for failing to follow a Tax Office private ruling? Do taxpayers only request PBRs when they are confident of a favourable ruling?

Not necessarily. There will always be some who attempt to manipulate the system. However, there should not be a penalty for failing to follow a ruling, there should only be a penalty for failing to comply with the legislation.

6 Response to Key Issues of Review-aspects of the operation of the General Interest Charge (GIC).

6.1 Should the GIC be set at a level to provide a positive incentive to encourage taxpayers to take steps to ensure they assess correctly? Or should this be dealt with exclusively under the penalty regime?

GIC should be set to compensate for the loss to the revenue. That is the time value of the money. The penalty provisions should ensure compliance. The current arrangement imposes two penalties. This is unfair.

6.2 Is the rate of the GIC excessive against this principle?

Yes.

6.3 Are the approaches identified in this Chapter suitable to address identified concerns with the GIC? If so, by what mechanism should the approaches be implemented? Are there cases where full GIC should continue to apply to shortfalls?

Yes, the approaches are suitable if genuinely applied.
There are no cases where full GIC should continue to apply.

6.4 What priority should be given to simplicity in considering any changes to the current GIC regime? Should different market segments be treated differently for GIC purposes? Is it feasible to move away from a single, comprehensive system?

The system is already too complicated – one policy should apply.

6.5 Should remission of the GIC be initiated by the Tax Office in more circumstances? If so, what criteria should be used?

Currently, GIC remission is only initiated by a request from the taxpayer and this is not generally known. Chapter 93 of the ATO Receivables Policy deals with GIC remission. Because the imposition of GIC is automatic, remission must be considered by the ATO in every case, otherwise taxpayers who deserve remission are likely to pay more than they should just because they were not aware that the GIC could have been remitted in their particular circumstances.

At the moment the ATO avoids responsibility and collects more GIC than is necessary by placing the responsibility on the taxpayer to initiate a request and then requiring the taxpayer to show overwhelming reasons why remission should occur. The ATO do not readily accept remissions reasons and generally refuse to remit unless forced to do so by political or public pressure.

In order to overcome the problems that currently exist with the imposition of GIC, the Commissioner must be required to document justification for non-remission of GIC; In other words the Commissioner must provide evidence of taxpayer wrongdoing in relation to the time period and the additional penalty component of the GIC. While the tax shortfall is the legislative trigger for imposition of the GIC, remission must also be automatic if the Commissioner does not provide evidence that the taxpayer fault caused the time delay. As a second step only necessary if there is taxpayer fault for the time delay the additional penalty rate should be remitted unless the Commissioner documents evidence that the taxpayer actions require a penalty. For example where the individual circumstances show deliberate evasion, then that same evidence will support non-remission of the penalty rate.
Commissioner's documentation of evidence to be reviewable by an independent panel without need to go to the AAT or the Federal Courts, especially in

circumstances where the primary tax may not be in dispute but the imposition of the penalty or GIC is disputed.

6.6 Should the benefit from tax deductibility of the GIC be standardised, to eliminate the impact of varying tax rates? If so, how should this be achieved?

No, there is enough confusion already. If anything GIC should not be deductible. At the moment the net effect is that the ATO receives more in one year and then repays a part of that amount later. There is no commercial benefit to impose a greater burden upon the taxpayer in one year only to repay an amount later. In some cases that marginal amount could be the difference between payment and dispute of the liability.
Also, in many cases taxpayers with outstanding disputes are claiming the GIC deduction when no payments have been made. In these cases the revenue is being lost, or at least the timing difference benefits the taxpayer.

6.7 What further steps would promote taxpayer awareness of their obligations under self assessment? Could, for example, notices of assessment be better labelled?

Self-assessment requires certainty from the administrator. Until the ATO knows what the legislation means it is unfair to expect the taxpayer to have the same level of knowledge. There must be more than labelling.

6.8 In what circumstances is there a need for a Public Tax Advocate or greater use of alternative dispute resolution?

In almost every case except those involving large multinational corporations with complex tax issues or those involving criminal activity.