

This document is the ATO's submission to the Australian Small Business and Family Enterprises Ombudsman (ASBFEO) review on early debt recovery action on a small business disputing a debt at the Administrative Appeals Tribunal (AAT).

This document is in response to information sought by the Australian Small Business and Family Enterprise Ombudsman.

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ATO Submission

review on early debt recovery action on a small
business disputing a debt at the AAT

The Australian Taxation Office (ATO) welcomes the opportunity to contribute to the Australian Small Business and Family Enterprises Ombudsman (ASBFEO) review on early debt recovery action on a small business disputing a debt at the Administrative Appeals Tribunal (AAT).

The ATO recognises the significant contribution small businesses make to the economy and the broader community, and we take pride in fostering positive engagement with the small business sector. We are committed to ensuring our actions and interventions through the course of administering the tax and superannuation systems do not disrupt the ability for viable small business to survive and thrive.

We understand that it is vitally important for us to demonstrate our ongoing commitment to improve the client experience. We are responding to reporting in the media about the unfair treatment of small businesses by us. Our taxation powers are largely aligned with those of other countries see [Tax Administration 2017 Comparative Information on OECD and Other Advanced and Emerging Economies](#). We recognise that the community's perception of whether we have treated taxpayers fairly and acted with integrity influences their willing participation in the tax and superannuation systems.

We remain open and receptive to feedback and scrutiny and use those sources of intelligence to help us make improvements. The Inspector General of Taxation (IGT) has recently completed their review into the *ATO's Use of Garnishee Notices* and the Australian National Audit Office (ANAO) is in the final stages of completing their audit on the *ATO's Management of Small Business Tax Debt*. We have adopted all recommendations from the IGT Review and adopt the majority of recommendations from external scrutineers. While important, we note our scrutineers are only one component of how the ATO makes decisions to improve the administration of the system. The majority of improvements are made as the result of our business-as-usual processes and collaboration with the community generally and through our specialised Stewardship Group advisory bodies.

Small Business by the numbers

For most ATO purposes, small businesses are those with an annual before tax turnover of under \$10 million.

There are approximately 3.8 million registered small businesses in Australia, including 1.6 million sole traders. They are diverse in structure (trusts, partnerships, companies, and various combinations of those), size, turnover, industry, location, number of employees (if any), maturity of business, acumen and understanding of tax, superannuation and other regulations.

In 2017-18, when we include related individuals, trusts, partnerships and companies, small businesses lodged around 5.4 million income tax returns and 12.2 million activity statements. Over 85% of small business taxes are paid on-time or within 90 days of the due date.

Over the course of 2017-18 financial year, of the 3.8 million small businesses, we undertook about 130,000 reviews, which included around 121,000 audits and 9,000 default assessments. Our audits related to issues including omitted income, PAYGW discrepancy

events, incorrect and incomplete obligation reporting (including GST obligations), non-lodgment, employer obligations and mistakes as a result of business structures.

From the 130,000 reviews reported as part of the ATO small business experience, there were about 68,000 cases where we issued an amended assessment – about 64,000 of those were undisputed, that is the taxpayer did not dispute the debt or lodge an objection.

In 2017-18 about 4,200 objections were received by our independent dispute resolution area in response to small business audit activity. In that year we allowed 2,650 objections in part or full and of these there were about 1,200 cases where the taxpayer provided information at objection which had been requested at audit but was not provided at that time.

In 2017-18 there were 143 Small Business appeals lodged on a taxation matter in the Administrative Appeals Tribunal (AAT). There were 108 cases that were resolved in the AAT in 2017-18. The 108 cases finalised in the AAT relate to a taxpayer flagged in the ATO's system as belonging to the small business experience. Of the 108 cases finalised, 24 went to AAT decision (of which 23 were determined in the ATO's favour wholly or in part).

For the vast majority of small businesses who have a disputed debt, we will not enforce recovery of a tax debt, including even parts of the debt which are not in dispute. The only time we will recover debts in dispute is in exceptional circumstances where we see evidence of phoenixing, fraud, criminality, serious tax evasion, dissipation of assets or transfer of funds to defeat the collection of tax. These are very rare cases. We can take action to collect outstanding tax irrespective of whether the tax is subject to an objection, review or appeal – this is allowed by law primarily to discourage misuse of the objections process simply to avoid or delay making payment and which might therefore clog the objection and appeals process to the disadvantage of honest small business operators with a genuine basis for review.

Disputed debt cases which are subject to debt recovery are assigned to specialist debt case managers who provide holistic risk based debt management tailored to the case at hand.

We do undertake automatic debt recovery action on undisputed amounts consistent with our policy Practice Statement Law Administration (PSLA) 2011/18 and 2011/4.

Responses to information requests

Scale

Information Request 1: *In 2017-18, the ATO website states 7,792 small business objections were lodged with the ATO. What percentage of these have been subject of debt recovery action, before resolution of the dispute (regardless of whether it is part of an internal or AAT review) and what is the overall level of disputed debt in these cases?*

ATO Response:

Responding to this question would require a manual review of all 7,792 cases and as such will not be available within your timeframe.

Information Request 2: Number of ATO initiated liquidations/bankruptcies

ATO Response:

Table 1: Bankruptcies – 2017-18 – All client groups

Bankruptcies – 2017-18 – All client groups	
Total bankruptcies	16,839
ATO-initiated	470
ATO-initiated % Total	2.8%

Table 2: Wind-ups – 2017-18 – All client groups

Wind-ups – 2017-18 – All client groups	
Total Wind-ups	8,375
ATO-initiated	1,282
ATO-initiated / Total	15.3%

Note up

1. Figures are point in time and subject to retrospective changes.
2. Bankruptcy information provided by the Australian Financial Security Authority (AFSA).
3. Wind-up information provided by the Australian Securities and Investments Commission (ASIC).

Information Request 3: The ATO website states that 478 applications for review are lodged with the Courts or tribunals.

- a) What percentage of these [small business cases] are lodged with the AAT
- b) What is the level of disputed debt [on small business cases] where recovery is initiated whilst still before AAT (with breakdown between tax, interest charges and penalties)
- c) When at the AAT, what is the number of [small business] cases where you commence debt recovery action and what is the number of [small business] cases where you continue debt recovery (i.e. commenced before AAT lodgement)
- d) When at AAT, how many [small business cases] proceed to winding-up or bankruptcy orders?

ATO Response:

- a) 72% (344) of all review applications were lodged with the AAT. 143 of the 344 review applications relate to an entity flagged in the ATO's system as a small business.
- b) There were three (3) cases where recovery was initiated while still before the AAT. The total level of disputed debt for these 3 cases was \$1,499,025.89, including

primary tax of \$844,560.41 and penalties totalling \$654,465.48. This figure is exclusive of General Interest Charge, which continues to accrue on a daily basis.

- c) When at the AAT, the ATO commenced debt recovery in the aforementioned 3 cases through the issue of a Notice of Intended Legal Action (a warning letter). The ATO continued debt recovery that had commenced before the AAT appeal being lodged in a further 14 cases i.e. bringing the total to 17 cases where debt recovery action was taken while the case was before the AAT. Note: each of these cases met the exceptional circumstances test or included significant undisputed debt amounts.
- d) When at the AAT, two cases, out of the 17, proceeded to winding-up or bankruptcy orders.
 - I. In the first case, the matter proceeded to the point where a winding-up order was made by the Court. This matter involved phoenixing and included both disputed and undisputed liabilities. The winding-up hearing was scheduled by the Court before the AAT appeal was lodged by the taxpayer. The Court decided to proceed with winding-up order in the full knowledge of the AAT appeal.
 - II. In the second case a bankruptcy order was made by the Court also while aware that the case was at the AAT. In this case, the taxpayer had a significant undisputed liability of around \$1m that was unpaid and there was no engagement by the taxpayer to address the liability.

Extent

Information Request 4: For matters before the AAT:

- a) *What is the number of matters where garnishee notices are used?*
- b) *What are the indicators that trigger a garnishee notice?*
- c) *What steps are taken to validate the indicators?*

ATO Response:

- a) For matters before the AAT, there were four cases, out of the 14 cases previously mentioned where recovery action continued after the AAT appeal was lodged, where garnishee notices were used.
- b) The ATO uses garnishees and pursues other debt recovery actions in disputed debt cases involving exceptional circumstances including phoenixing, fraud, criminality, serious tax evasion or evidence of the actual or likely dissipation of assets or transfer of funds to defeat the collection of tax. Risks involved in these specific four cases involving use of garnishee notices after an appeal was lodged at the AAT were as follows:
 - I. One case where the taxpayer was involved in criminal activity that was referred from Australian Customs and Border Protection. There was also evidence of asset dissipation.
 - II. One case involving a tax agent with evidence of fraud and evasion, significant non-compliance with tax obligations and failure to deal with undisputed liabilities. The taxpayer dissipated assets during the dispute.

- III. One case involved a taxpayer with a history of non-lodgement, significant undisclosed income and who had failed to engage to address outstanding undisputed liabilities. The taxpayer continued to purchase assets without addressing his undisputed liabilities and a garnishee was issued with the intention of applying proceeds towards the undisputed liability.
 - IV. In one case, a point in time garnishee issued against a taxpayer and resulted in a collection of around \$2,000 (against a liability which on conclusion before the AAT was around \$100,000). This was due to the disputed debt indicator not being set in this one case.
- c) No automated debt recovery action is applied to an account which includes a disputed debt.

Where there is disputed debt with exceptional circumstances, these cases are subject to active case management by a specialist debt collection team. The risk is informed by the characteristics and behaviours of the client, at audit and during debt recovery, as well as the need to protect revenue, while being cognisant of the appeal or court process and the ATO's obligations as a model litigant.

Active debt case management adheres to standard ATO policies (as further detailed in response to question 5) and includes the following additional validation processes:

- I. A dedicated case manager is assigned to the case. The case manager uses a range of information and research processes to become intimately familiar with the case, including the risk factors, asset and income position of the taxpayer, their capacity to pay and their inclination to do so.
- II. The dedicated case manager is also directly involved in discussions and negotiations with the taxpayer and/or the taxpayer's representative in relation to the payment of the debt (to the extent the taxpayer is willing to engage in such discussions). While conduct of the appeal is managed by the Review and Dispute Resolution (RDR) team, the case manager also works closely with RDR as well as the referring audit staff to fully understand the risks and issues present in the case.
- III. Case managers work within a specialist case management team with oversight via mechanisms such as case management planning reviews and case call overs with senior staff, including a cohort of highly experienced specialised technical advisors.
- IV. While case managers exercise their own judgement when considering the risks and options in the case, this is done with appropriate support, consultation and oversight from senior staff.

Impact

Information Request 5: *What steps are taken to document and assess the potential impact of a garnishee notice or other debt recovery instrument on a small business taxpayer? (such as, inability to pay suppliers and staff, insolvency, inability to pay family living expenses etc.)*

ATO Response:

In all matters, disputes or otherwise, staff follow the policy statement (PSLA 2011/18) to consider:

- the financial position of the tax debtor and the steps taken to make payment in the shortest possible timeframe having regard to the particular circumstances of the tax debtor
- the extent of any other debts owed by the tax debtor
- whether the revenue is placed at risk because of the actions of the tax debtor, such as the tax debtor making payment to other creditors in preference to paying the Commissioner
- the likely implications of issuing a notice on a tax debtor's ability to provide for a family or to maintain the viability of a business.

Further to this, the procedures require staff to consider the following when issuing a garnishee:

- whether the client is at the forefront of the ATO officer's thinking, as opposed to just following a process
- the financial position of the client and the steps taken to make payment in the shortest possible timeframe having regard to the particular circumstances of the client
- the extent of any other debts owed by the client, and the implications for the client's creditors if our garnishee action is successful
- whether the revenue is placed at risk because of the actions of the client, such as the client making payment to other creditors in preference to paying the Commissioner
- the likely implications of issuing a notice on a tax debtor's ability to provide for a family or to maintain the viability of a business
- the consequences of inappropriate/invalid garnishee action for this client
- whether every reasonable effort has been made to contact the client directly.

The requirement to make every reasonable effort to contact the client directly gives us the opportunity to determine the financial situation of the client. It is through these discussions that clients are made aware of their obligations and the consequences of failing to meet these obligations. These conversations also allow clients to provide insights to their current financial position.

Where these contacts are unsuccessful (i.e. no contact or no information is provided by the client as per their financial position) staff may still consider the above criteria and make the decision to issue a garnishee notice.

To mitigate the risk of the notice affecting the taxpayer's ability to provide for a family or the viability of the business the following procedural requirements restrict the impact of the notice:

1. Notices to Taxable Payments Annual Report (TPAR) - notices may be set as an ongoing % - where 15% is the recommended rate (or 5% for clients paying their ongoing liabilities) or for a fixed amount. This % may be varied. Where any change to this % is required approval is obtained from the staff's manager;

2. Notices to employers - the recommend rate is 10% of the gross wage. This % may be varied. Where any change to this % is required approval is obtained from the staff's manager;
3. Notices to financial institutions (not including merchant facilities) - Point in time garnishees (requiring payment of the full debt amount or 30% (variable) of the bank balance, whichever is lower) are issued in most instances. In extreme circumstances a standard garnishee may be issued;
4. Notices to Merchant facilities - notices may be set as an ongoing % - where 15% is the recommended rate (or 5% for clients paying their ongoing liabilities);
5. Notices to other third parties - notices may be set as an ongoing % - where 15% is the recommended rate (or 5% for clients paying their ongoing liabilities) or for a fixed amount. This % may be varied, where any change to this % is required approval is obtained from the staff's manager.

To assist staff in determining the appropriate outcome the client's history is reviewed. Also data is sourced from a Risk Assessment Profiling Tool.

This data includes (not exhaustively):

- TPAR payments received per previous FY
- Identifiable interest payment amounts
- PAYG annual statements
- Merchant facility providers and amounts paid
- Government payments
- Dividends
- BAS cash flow
- Debt trends

Staff are able to use this information and their professional judgment to identify an appropriate garnishee source and creating an appropriate notice that satisfies the criteria above.

Information Request 6: *Do you refer small business taxpayers to support services (such as financial counselling, mental health etc.)?*

ATO Response:

We encourage small business owners who are having difficulties meeting their tax and super commitments or struggling with their mental health to contact us. Depending on their individual circumstances, we offer a range of help and support services including

- tailored payment plans
- lodgment and payment deferrals
- priority processing of tax return refunds
- after hours call back
- personalised business assistance.

Our website has more information for small business owners experiencing mental health issues – ato.gov.au/smallbizmentalhealth.

All ATO frontline and client contact staff must complete this training as part of the ATO's Mental Health Strategy. We provide our staff with training and tools to recognise the signs of mental illness and where to refer taxpayers for additional support.

Our staff refer clients (when necessary) to mental health services including:

- Beyond Blue support Services
- Suicide Call back Service
- Lifeline Counselling Service
- Men's Help Line

Dispute Assist

Taxpayers can access additional support through Dispute Assist when they are in dispute with us. This is a free service to help unrepresented individuals and small businesses with the dispute process.

We recognise some taxpayers involved in an objection or dispute process may be at a disadvantage. Significant or exceptional personal circumstances and the inability to afford representation may contribute to being in dispute.

The service was trialled in 2017 and received positive feedback from taxpayers, showing Dispute Assist made the process easier.

Dispute Assist can support small businesses when:

- an objection is lodged
- the objection (dispute) isn't lodged by a formal representative (for example, an accountant, tax agent or legal representative)
- the taxpayer indicates they are suffering from significant or exceptional circumstances.

Support is provided by an experienced Dispute Assist Guide who is completely independent from the objection or dispute process.

Independent Dispute Assist Guides help taxpayers through the dispute process and work towards resolving the dispute by:

- connecting the taxpayer with the right people so the dispute can be resolved as early as possible
- ensuring all options have been explored in resolving the dispute
- providing assurance that the dispute has been handled fairly, and
- assisting the taxpayer to access services to help them move forward.

Dispute Assist has supported 75 small business taxpayers in 2017-18. To date this year we have assisted 65 taxpayers.

Our Independent Dispute Assist Guides receive mental health training and regularly refer taxpayers to the external support services including those listed above.

Dispute Assist is displayed prominently on the Small Business Newsroom Site (over 2.5m subscribers) and relevant content is available on our [website](#). We have amended the objection form to offer clients the opportunity to request the service. We have also distributed

our flyer to many organisations that offer support services for those experiencing mental health or financial difficulties.

Closing

We are receptive to hearing and addressing concerns regarding our administrative approaches for small businesses, to understand how we can improve these approaches.

The information contained in this submission is to provide context for the system in practice. Our priority is to do what we can to maintain community confidence, and particularly to ensure that we retain small business confidence in our administration of the tax and superannuation laws. Our administrative approach is to be appropriate, empathetic, fair and is characterised by integrity.

Reviewing individual cases

If there are specific cases ASBFEO would like investigated we are happy to ask the IGT to independently review them. While the IGT could not provide specific details to ASBFEO, they could assess that they met the “exceptional circumstances” test. The IGT will also be able to provide independent assurance about the ATO’s exercise of its powers demonstrating that they are consistent with ATO policies and procedures. If the IGT identifies any cases that don’t meet the exceptional circumstances test, we want to know about them, so we can understand what happened and improve our approach.

Appendices

[Appendix 01 - ATO Powers](#)

[Appendix 02 - Our approach is to resolve disputes](#)

[Appendix 03 - Our approach to managing debt](#)

Appendix 01- ATO Powers

The ATO takes all steps to ensure we exercise our powers in the administration of the tax and superannuation systems judiciously, with sensitivity to individual client circumstances and with appropriate discretion. The powers afforded to the ATO in this regard are comparable with those of other tax administrations internationally. There are widely recognised policy drivers for tax administration powers to be set in this way. A range of robust governance controls exist to ensure the ATO exercises its powers appropriately and proportionately. These controls include the regulatory environment we must comply with, external scrutineers, Parliamentary hearings and examination. These sources of external scrutiny are bolstered by the ATO's internal committee structures including our Audit and Risk Committee, Senior ATO Executive oversight and a comprehensive framework of internal processes and procedures, quality assurances and analysis of our complaints feedback to ensure the necessary checks and balances are in place.

Our activities are geared towards ensuring taxpayers willingly comply with their obligations under the tax and superannuation laws relevant to their circumstances, that a level playing field is preserved for all taxpayers in the system and the community's trust and confidence in our administration is upheld. Our approaches to engender trust and confidence centre on taxpayers who are doing the right thing are supported, and the vast majority of taxpayers who exercise appropriate diligence in meeting their obligations can see that action is taken with taxpayers who fail to participate correctly and they are brought to account.

Appendix 02 - Our approach is to resolve disputes

The vast majority of interactions with small business result do not result in a dispute and there is no evidence to suggest systemic issues with the engagement the ATO has with small business. The IGT' recent review of our use of garnishee notices is evidence of this. The need for engagement with small business beyond their cyclical lodgement and payment obligations is very much the exception rather than the rule. In the relatively small number of cases that do result in a dispute, we acknowledge that there are occasions where we don't always get things right. We are focused on ensuring we have the right mechanisms in place to surface any such instances as quickly as possible, and for these to be resolved through constructive engagement and resolution between the ATO and the taxpayer rather than on a dispute footing. We strive to do better in this area by more quickly recognising our error.

Nevertheless, the experience of tax administration here and elsewhere around the world is that some level of disputation is inevitable. Where a small business taxpayer disagrees with our assessment, they can seek a review of the decision by lodging an objection in writing. That objection is determined by an independent area (the ATO's review and dispute business line (RDR) within the ATO entirely separate from the original audit decision making that area. This independent area already reports to a separate Second Commissioner ensuring the review of the decision is always independent of the original decision maker. We believe the best strategy for resolving disputes it to prevent the dispute from arising in the first place and where that is not possible, trying to reach resolution as soon as possible.

If the small business disagrees with the outcome of the objection they have the option of pursuing action at a relatively low cost through review in the Administrative Appeals Tribunal, or alternatively they can have their matter referred to the Federal Court of Australia if they wish. However, we acknowledge that in any dispute there is also personal time and effort for each party to be factored in.

The RDR objection review function has been functionally separate and independent from ATO audit areas since 1 July 2015. Communication protocols are in place to ensure RDR officers remain independent from original decision making areas of the ATO during an objection review.

RDR, along with the entire ATO, promotes a culture of fairness in dispute resolution. Fairness is promoted from both the perspectives of outcome and procedure. This approach has included ensuring that our people contact the client by phone as soon as possible once we've received their objection to discuss the timeframe for the resolution of their dispute while considering the client's circumstances and issue.

In majority of our review interactions with small business clients, the client has a tax agent and we work collaboratively with that advisor and the client, to try to resolve disputes as early as possible. As part of our commitment to fair, impartial and effective dispute resolution, RDR has a number of dispute resolution services, which are all free, to assist taxpayers in dispute with the ATO. These include:

- Independent Review
- In-House Facilitation (IHF) - which can occur on premises for small business if preferred by the taxpayer
- Independent Assurance of Settlements
- Dispute Assist

The Role of the AAT

Where a taxpayer disagrees with the ATO's decision on a tax objection they can seek external review of the merits of that decision in the AAT or the Federal Court of Australia.

The AAT is an independent body established by statute to review a range of administrative decisions on the merits, including tax objection decisions. AAT proceedings are less formal and less costly than a court case. Taxpayers, including small businesses, can represent themselves or be represented by their tax advisor, lawyer or some other representative. Costs orders cannot be made so each party pays their own costs. This means a small business can request a review in the Tribunal knowing that it will not be exposed to an order to pay the ATO's costs if it is unsuccessful. Once the taxpayer has applied to the Tribunal the ATO has an obligation to provide all documents relevant to the disputed decision to the Tribunal.

Recent initiatives to support small business

On 1 March 2019, the Small Business Taxation Division of the AAT commenced. The role of the ATO in these proceedings is to assist the Tribunal with its review of the decision. In assisting the Tribunal, the ATO will be represented by ATO officers from RDR, who will typically be junior lawyers. The ATO will not be represented by external lawyers, other than in exceptional circumstances. Other than in those cases where the small business or Tribunal object, the ATO will seek to include the original decision maker as a participant in the proceedings. This will ensure the decision maker remains accountable for the original decision and can learn from hearing the observations of the Tribunal and the taxpayer.

In the exceptional circumstances where we do use an external lawyer or counsel, the ATO will provide funding to an unrepresented taxpayer for their reasonable legal expenses to ensure they can obtain equivalent legal representation. The funding for reasonable costs of the taxpayer's legal representatives will be determined consistent with the way in which these costs are already determined for cases that receive test case funding.

Where a decision of the new Division is appealed by the ATO to the Federal Court, the ATO will fund the taxpayer's legal representation on a reasonable costs basis. We will not enforce recovery of a tax debt in dispute before the new Division other than in exceptional circumstances.

National Tax Clinics Trials

The ATO provides local liaison and escalation assistance to the Curtin University Tax Clinic which provides general taxation advice and help to individuals and small businesses with their tax obligations and reporting requirements. The Curtin Clinic has helped over 180 taxpayers so far.

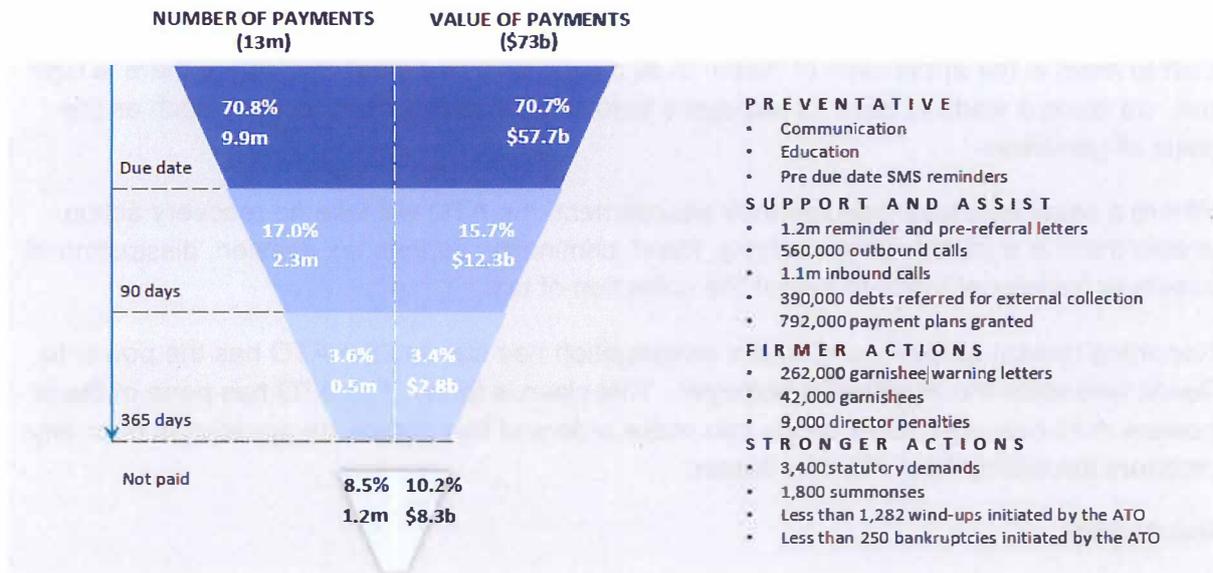
On 28 November 2018, the Government announced the National Tax Clinic Trial which will see the establishment of a further nine tax clinics in early 2019.

Appendix 03 - Our approach to managing debt

Our approach to debt management is to focus on prevention and support, with these combined actions seeing 96% of tax debt across all market segments paid on time or within 90 days after the due date. To achieve this, we make it as easy as possible for taxpayers to pay their tax on time using a wide range of tools through our online services such as the Payment Plan estimator, payment channels and self-serve payment options which can also be accessed over the phone. These services enable taxpayers to work out a plan that meets their circumstances, taking into account the payment plan conditions and their capacity to pay off the debt including interest. Illustrating the scale of our prevention and support interactions for small business, in 2017-18, we received over 1.1 million calls, made a further 560,000 calls and sent 1.2 million reminder and pre-referral letters.

Figure 1. 2017-18 Small Business

2017-18 SMALL BUSINESS



We recognise that taxpayers may occasionally experience short term cash flow issues that prevent them paying on time. We assist by offering payment plans tailored to their individual circumstances – granting 1.1 million arrangements in 2017-18, of which 792,000 were for small business. We also recognise that taxpayers can experience longer term financial difficulties due to challenging economic conditions or unexpected events. We take an empathetic approach to working with these taxpayers to get them back on track, for example through more generous payment arrangements and consideration of penalty and interest remission.

Through our Reinvention Program, the ATO has focused on ways to make it easy for taxpayers to comply and hard not to. From an education, prevention and support perspective, an example of the support we provide is the Cash Flow Coaching Kit. This educational coaching program was co-designed with tax professionals and small business to increase business and financial acumen by helping small businesses understand and improve their cash flow and provisioning to meet their commitments.

Where taxpayers experience serious hardship we provide targeted support using a range of debt relief options, including release from payment in some cases.

If a small business chooses not to engage with us around their tax debt, we will follow up and if repeated attempts to re-engage them fail, we may be left with no other option but to take firmer action to ensure the debt is paid such as issuing garnishees and director penalty notices.

As a final step we may take stronger debt recovery actions, including making a formal demand for payment through the Court, and finally possibly initiating insolvency (which is also decided by a Court). In particular we may take this action when a business is continuing to trade (possibly while insolvent), incurring new debts (to employees, suppliers, other creditors and the ATO) and is thereby gaining an unfair financial advantage over competing small businesses who are meeting their obligations.

In vast majority of cases we use stronger action like garnishees and insolvency proceedings when taxpayers refuse to engage with us and don't deal with their tax debt over a period of time. Garnishees are not automatically applied and there are no revenue targets for ATO staff to meet in the application of these. In all cases, except a small few where there is high risk, we issue a warning letter to taxpayers before undertaking firmer actions such as the issue of garnishee.

Where a small business disputes their assessment, the ATO will take no recovery action unless there is evidence of phoenixing, fraud, criminality, serious tax evasion, dissipation of assets or transfer of funds to defeat the collection of tax.

Reporting related to the Four Corners investigation has claimed the ATO has the power to freeze and seize the assets of a taxpayer. This claim is false. The ATO has none of these powers in its own right. Only courts can make orders of this nature, on application from any creditors (including the ATO) of a debtor.

Insolvency

In insolvency tax debts have no special priority. The ATO sits at the back of the queue along with any other unsecured creditors. The notable exceptions to this are

- superannuation guarantee charge debts which the ATO collects on behalf of employees – these debts have the same priority ranking as other employee entitlements such as unpaid wages
- in a very limited number of cases a taxpayer may have voluntarily entered into a security arrangement with the ATO, e.g. offering security over a property to help the taxpayer manage their liquidity when dealing with a large tax debt

The ATO-initiated around 1,280 wind-ups and less than 250 bankruptcies relating to small businesses last financial year.

Review of ATO decisions to enforce insolvency

In June 2018, an independent external review of our insolvency cases concluded our collection practices do not prematurely lead to viable taxpayers being made insolvent. This is the fifth time this external review has taken place and in each instance the independent reviewers have never found a case where we acted prematurely.

The full report is included below.

<https://www.ato.gov.au/About-ATO/Commitments-and-reporting/In-detail/Debt-recovery---review-of-ATO-decisions/Independent-review-of-ATO-decisions/Review-of-ATO-decisions-to-enforce-insolvency--June-2018/>

Attachment A: 2018 Insolvency Review

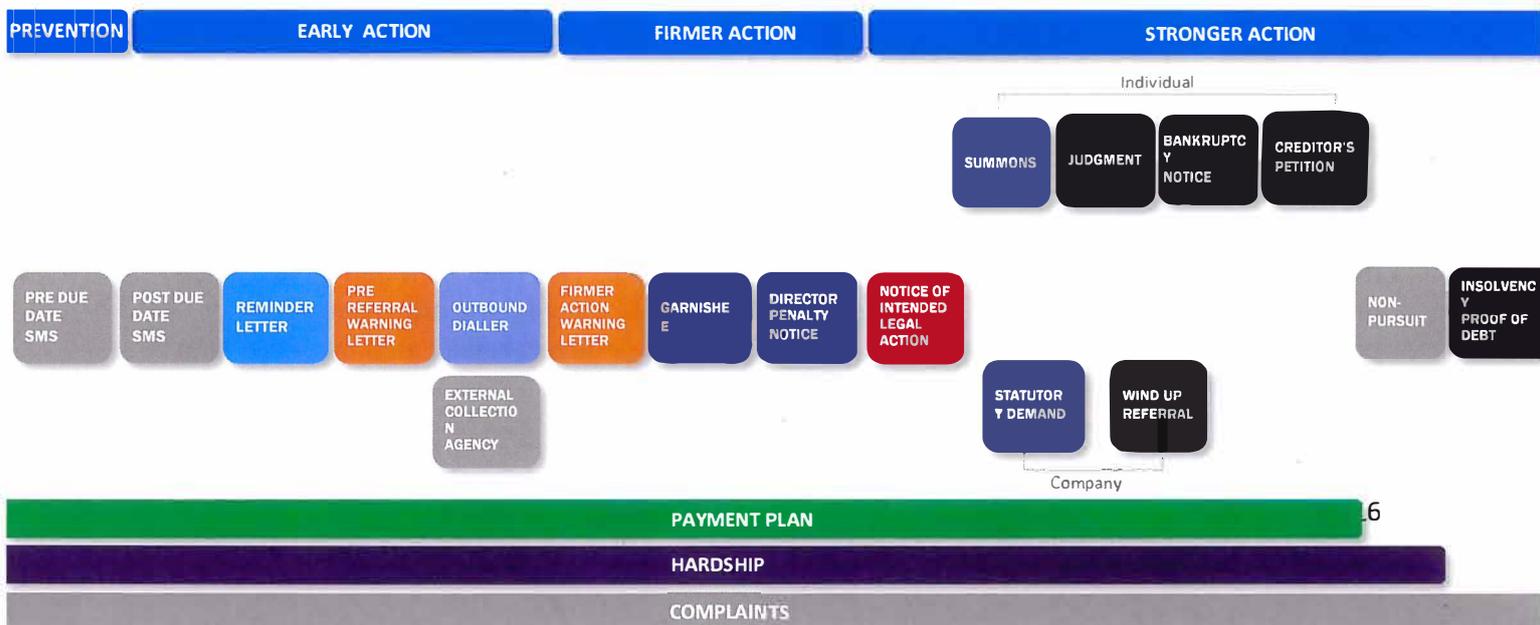


Review_of
ATO_decisions_to_er

Flow of debt cases

This diagram provides an overview of the debt collection cycle. While it appears linear, not all debt cases will progress sequentially through each collection activity as we increase our use of analytics to better tailor our services and contact with taxpayers. This approach uses payment experience models that consider client characteristics and behaviours and then determines the most appropriate action to engage the client and resolve their liability (e.g. we do not send another overdue reminder letter to a taxpayer with an escalating debt who has repeatedly ignored previous letters).

Figure 2. Flow of debt cases



Steps to ensure recovery actions are appropriate

We take a purposeful approach to payment and debt, balancing support for clients trying to do the right thing with timely stronger action against those who don't engage to prevent them gaining an unfair financial advantage. There are no revenue targets for staff undertaking this work.

Our debt management approach is set out in our policy documents. This includes our approach to issuing garnishee notices and other firmer recovery actions. Our approach is as follows:

Step 1. Prevention of debt – by educating, and communicating with taxpayers, about their obligations, and how to meet them. As part of this approach, we issue text message reminders to some taxpayers before their debts fall due.

Step 2. Support and assistance – to help taxpayers get their tax and super debts back on track as soon as possible. This includes:

- issuing debt reminder letters and text messages, as well as calling taxpayers
- payment plans available as self-help options online and over the phone, to help taxpayers manage their debts where they are unable to pay in full immediately
- hardship provisions assist those taxpayers having difficulty paying, enabling them to obtain payment extensions, penalties and interest waivers and, in limited circumstances, compromise or forgiveness of debts
- Note - Payment plans and consideration of hardship is available all the way through the debt recovery process, up until final insolvency – flow of debt cases in *Figure 2. Flow of debt cases*

Step 3. Firmer action – to pursue those who fail to engage with us. This includes:

- issuing garnishee notices to third parties
- issuing director penalty notices, where directors are personally liable for the debts of their company.

Step 4. Stronger action – this includes making application to the court to commence:

- legal recovery
- insolvency proceedings

Garnishees – approach and safeguards

Where our text messages, phone calls and letters have issued and the taxpayer continues not to engage with us to pay their debts, we then consider what action to take. The issuing of a garnishee is not an automated process. As the Inspector-General of Taxation noted in their recent review, our debt collection officers follow processes and procedures and exercise their judgment to determine what action is most appropriate. This may be a garnishee notice or other approach. Staff issuing garnishees must complete training and adhere to ATO policies and procedures. Debt delegation and authorisation levels reflect staff capability and remove unnecessary escalations.

Except in a small number of high risk cases, taxpayers will receive a warning notification (most commonly a letter) advising the next steps we may take (which include garnishee) and giving them a further opportunity to address their debt before we take firmer debt collection action. Firmer action will not take place unless the taxpayer fails to engage with us to address their debt after they receive the warning notification.

Collecting disputed debt

For the vast majority of small businesses who have a disputed debt, we will not enforce recovery of a tax debt, including even parts of the debt which are not in dispute. The only time we will recover debts in dispute is where we see evidence of phoenixing, fraud, criminality, serious tax evasion, dissipation of assets or transfer of funds to defeat the collection of tax. These are very rare cases. We can take action to collect outstanding tax irrespective of whether the tax is subject to an objection, review or appeal – this is allowed by law primarily to discourage misuse of the objections process simply to avoid or delay making payment and which might therefore clog the objection and appeals process to the disadvantage of honest small business operators with a genuine basis for review.

Disputed debt cases which are subject to debt recovery are assigned to specialist debt case managers who provide holistic risk based debt management tailored to the case at hand.

Freezing, seizing and selling assets

A freezing order prevents a person or company from dealing with its assets. Freezing orders and seizure orders are exclusively issued by the courts. While the ATO applies for a handful of freezing orders each year, we have no independent power to issue a freezing order.

Another right generally available to any creditor via application to a court is to seek a warrant of seizure (also known in some states as a writ of execution or an enforcement warrant) which allows a bailiff or sheriff to seize property and realise its value to pay a court judged debt. The ATO does not currently use this standard right of a creditor in our routine debt collection process.

A taxpayer may enter into an arrangement with the ATO to offer security over a debt. The ATO may seek such an arrangement from a taxpayer where we perceive a specific risk such as asset dissipation. Equally a taxpayer may wish to enter into such an arrangement to give the ATO certainty of collection and hence allow us to defer recovery action. A taxpayer may wish to do this if they have illiquid assets or need time to sell a business or property. ATO security arrangements are a low impact recovery option for taxpayers, and preferable to alternatives such as bankruptcy. Historically the ATO has appointed receivers to liquidate a security (i.e. sell an asset) in about 3% of secured arrangements.

