

Grant

The Parliament of the Commonwealth of Australia
Joint Committee of Public Accounts

Report No. 326

An Assessment of Tax

A Report on an Inquiry into the
Australian Taxation Office

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- 1 Appointed 19 August 1993
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 - 4 Appointed 19 August 1993
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 - 6 Discharged 17 August 1993
 - 7 Appointed 5 July 1993, Discharged 19 August 1993

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8. Appointed 6 March 1991

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Section 8(1) of the Public Accounts Committee Act 1951 reads as follows:

- (a) to examine the accounts of the receipts and expenditure of the Commonwealth including the financial statements transmitted to the Auditor-General under sub-section (4) of section 50 of the Audit Act 1901;
- (aa) to examine the financial affairs of authorities of the Commonwealth to which this Act applies and of inter-governmental bodies to which this Act applies;
- (ab) to examine all reports of the Auditor-General (including reports of the results of efficiency audits) copies of which have been laid before the Houses of the Parliament;
- (b) to report to both Houses of the Parliament, with such comment as it thinks fit, any items or matters in those accounts, statements and reports, or any circumstances connected with them, to which the Committee is of the opinion that the attention of the Parliament should be directed;
- (c) to report to both Houses of the Parliament, any alteration which the Committee thinks desirable in the form of the public accounts or in the method of keeping them, or in the mode of receipt, control, issue or payment of public moneys; and
- (d) to inquire into any question in connexion with the public accounts which is referred to it by either House of the Parliament, and to report to that House upon that question,

and include such other duties as are assigned to the Committee by Joint Standing Orders approved by both Houses of the Parliament.

PREFACE

This Report presents the Committee's findings from its Inquiry into the Australian Taxation Office (ATO) and so is 'An Assessment of Tax'. The Inquiry was the first major public examination of the manner in which taxation laws are administered in Australia since the passing of the *Income Tax Assessment Act 1936*.

The administration of taxation is an on-going and everchanging process and throughout the Inquiry the Committee has recognised the fact that changes have been occurring continually in both the administration of the ATO and the processes for collecting tax. Analysis on an historic or static basis has therefore not been possible and the Committee has consequently sought to examine the ATO's system of administration at a general level. However, where necessary, the Committee has commented on specific subjects which were drawn to its attention in the course of the Inquiry.

As an inquiry into administration, the Committee's terms of reference did not provide for either the consideration of the policy underlying the tax law or the economic basis of the law. Nevertheless, the line separating policy and administration is often blurred and, to the extent that the ATO's administration is critical to the effective implementation of taxation policy, the Committee has given consideration to the efficiency of a number of the current statutory provisions. I would add that, while the Committee has not evaluated the circumstances of individual taxpayers, it has used a number of the cases presented to it in evidence to highlight its general findings.

The ATO is alone responsible for income tax collection, has been given exceptional powers and plays a vitally important role in the efficiency of the Australian economy. This accentuates the importance of establishing an administration which is fair, equitable and sufficiently flexible to manage the individuality of taxpayers. In this context, the Committee views the use of the term 'client' to describe taxpayers as misleading. In this report the Committee seeks to introduce balance to the current system which it sees as having grown to ignore the people it serves.

There are inherent difficulties in the administration of an organisation of 18 000 people, which has responsibility for the expenditure of over \$1 billion and the collection of revenue from over 10 million citizens. Nevertheless, the Committee considers such factors cannot be allowed to excuse, explain or even justify those circumstances where the system overwhelms the individual. I note that, while there are scathing criticisms levelled at the ATO, there are those in the community who recognise the organisation is focussing on the key areas of revenue loss. The public perception of the ATO remains one of the organisation's greatest challenges. Time alone will not alter those perceptions.

The Inquiry was commenced in the 36th Parliament but not completed before the March 1993 federal election. At the commencement of the current Parliament, the Committee determined to resume and complete the Inquiry. To allow new members of the Committee to familiarise themselves with the subject and update relevant information, the Committee conducted two public hearings during 1993 with witnesses from the ATO, including the newly appointed Commissioner of Taxation, Mr Michael Carmody.

On behalf of the Committee I acknowledge the assistance and cooperation provided during the Inquiry by Commissioner Carmody, his predecessor, Mr Trevor Boucher, and the staff of the ATO. The Committee wishes to express its appreciation to those officers of the ATO who appeared before it.

I take this opportunity to thank my predecessor, the Hon Gary Punch, MP, the former Vice Chairman, Senator John Watson, and all members of the Seventeenth Committee and the current Committee for their contributions.

On behalf of the Committee I record our gratitude for the work and support provided by our Secretary, Mr Trevor Rowe, and his dedicated staff. We are particularly appreciative of the assistance provided by Mr Simon Edwards who, with the cooperation of his department, the Department of Finance, was seconded to the secretariat for the greater part of the Inquiry. Finally, I would like to acknowledge the valuable contribution made by Mr Peter Dowling, a partner with Ernst & Young in Brisbane, who acted as a technical adviser to the Committee during its finalisation of the Report.

For and on behalf of the Committee,

L J Scott, MP
Chairman

CONTENTS

Chapter	Page
. Duties of the Committee	vi
. Preface	vii
. Contents	ix
. Appendices	xv
. List of Figures	xvi
. List of Tables	xvi
. Executive Summary	xviii
. Recommendations	xxiv
. Abbreviations	xlili

PART 1 - PRINCIPAL ISSUES

1. INTRODUCTION

. Background	3
. Terms of Reference	4
. Conduct of the Inquiry	4
. The Evidence	5
. Structure of the Report	6

2. HISTORICAL BACKGROUND

. Introduction	7
. 1910 - 1960	7
. 1960 - 1980	13
. 1980 - 1992	17

3. ADMINISTRATIVE STRUCTURES

. Current Administrative Structures	28
- Program Structure	28
. Efficiency of the Current Administrative and Organisational Structures	31
- National Program and Group Structure	34
- Social Objectives and the Changing Role of the Australian Taxation Office	35
- Internationalisation of the Australian Economy	36
. Senior Management Structure - Proposals for Change	37

.	International Comparison	41
-	United States of America Internal Revenue Service	42
-	United Kingdom Board of Inland Revenue	43
.	Revised Management Structure	44
-	Role of Chief Commissioner	44
-	Accountability	46
-	Reporting Requirements	49
.	Second Commissioners	50
.	National Program Managers	51
.	Deputy Commissioners	52
.	External Advice	54
-	Tax Liaison Group	55
-	Commissioner's Advisory Panel	56
-	Relationship between Advisory Committee and Australian Taxation Office Staff	58
-	Conflict of Interest	59
-	Duality of Operation	60
4.	SELF ASSESSMENT	
.	History of Self Assessment	63
.	Efficiency and Effectiveness	66
.	Costs of Compliance	71
.	Proposals to Extend Self Assessment	73
5.	LEGISLATIVE FRAMEWORK	
.	Introduction	75
.	Problems with the Current Act	76
-	Complexity	76
-	Uncertainty	77
-	Problem of Expression	78
.	Administering the Unadministerable	79
.	Self Assessment	80
.	Cost of Compliance	81
.	Rewriting the Act	81
-	Legislative Drafting Process	85
.	Proposals for Change	88
-	Economic and Administrative Policy Integration	89
-	Tax Impact Statement	90
-	Parliamentary Counsel	92

6. RULINGS

. The Taxation Rulings System	95
. Preparation	99
. Supervision of Public Rulings	105
- Tabling and Disallowance	109
. Private Rulings	113
. Determinations	116
. Rulings and Legislative Change	117
. Consistency of Rulings	118
. Timeliness	119
- Prospective v Retrospective	119
. Obsolete Rulings	121

7. MODERNISATION

. Introduction	123
. Background	123
. Systems Re-equipment and Redevelopment	126
. Electronic Lodgement Service	129
- Automated Document Dispatch	132
- Tax Local Area Network	133
. Automated Data Capture	135
- National Office Management Administration System	136
. Decentralisation	137
. Role of Staff in Modernisation	140
. Specialist Cells	140
. Modernisation Agreements	143
- PSU Moderation Agreement	143
- The Funding Agreement	144
. Modernisation - The Future	147

8. RESOURCES

. Running Costs	149
- Definition	150
. Human Resources	151
- Salaries and Staff	151
- Staff Morale	156
- Staff Skills and Training	157
- Technical and Skills Based Training	160
- Interaction with the Private Sector	162
- The Use of Retired Staff	163
- Future Priority Requirements	164
. Administrative Expenses	165

. Property	171
. Legal Services	172
. Other Services	173
. The Efficiency Dividend	174
. Income Tax Compliance/Enforcement Strategy	176
- Large/Medium Business Segment	178
- Small Business	179
- Non-business Individuals	181
. Projected Revenue Gains and Resource Requirements	182
- Absolute Value of Revenue Collections	182
- Basis of Revenue Collection	183
- Revenue by Segment	184
- Resources for the Strategy	186
- Special Audit (Criminal Activities)	187
. The ATO and the Department of Finance	188

PART 2 - ATO OPERATIONS AND TAXPAYERS

9. REVENUE COLLECTION

. The Revenue Collection Group	193
. Efficiency of Collection	200
. Processing Returns	203
. Revenue Collection Strategies	205
. Revenue Collection Systems	206
- Pay-As-You-Earn	206
- Prescribed Payments System	207
- Provisional Tax System	207
- Other Collection Approaches	208
- Debt Collection	211
- Fringe Benefits Tax Audit	216
- Additional Funding for Revenue Raising Activities	220
. Hardship	221
. Relief Board	223

10. TAXPAYERS ASSISTANCE

. Oral Advice	226
. Written Advice	232
. TaxPack	233
. Information Brochures	235
. Written Agreements	235
. Other Forms of Advice	236
. Role of the Tax Agents and Advisers	238

11. AUDITING

. Introduction	241
. The Taxpayer Audit Group	242
. The Principles of Taxation Audit	245
. Risk Management and Case Selection	247
. Information for Case Selection	252
- Conclusion	255
. Types of Audit	256
. Current Year Audits	260
. The Roles of the Auditor	261
. Investigation and Information Collection	262
. Analysis and Interpretation	265
. Assessment	271
. Audit Settlement	280
. The Costs and Benefits of Auditing	282
. Audit Resources	283
. Length of Audits	286
- Finalisation of Audit	287
- Special Audit	288
. Auditing of Restricted Access Status Taxpayers (RAST)	288

12. ENFORCEMENT AND PENALTIES

. Causes of Non-Compliance	291
. Detection of Non-Compliance	292
. Interest	295
. Late Payment Penalty	296
- Transition Arrangements	296
. Culpability Penalties	296
. Prosecutions	300
. Double Jeopardy	303

PART 3 - TAXPAYERS AND THE ATO

13. TAXPAYERS' CHARTER

. The United Kingdom Citizen's Charter	308
. The United States' Taxpayers' Advocate	309
. Taxpayers' Charter	310
. Taxation Ombudsman	314
. Taxpayer Privilege	318

14. AVENUES OF REVIEW

. Avenues of Review	323
. Right of Review - Objections	324
. Internal Review - Appeals and Review Group	325
. External Review	326
. Reporting by the Administrative Appeals Tribunal	332
. Cases Before the Federal Court	333
. The Australian Taxation Office as a Litigant	335

APPENDICES

Appendix	Page
1. SUBMISSIONS TO THE INQUIRY	339
2. PUBLIC HEARINGS - WITNESSES TO THE INQUIRY	345
3. EXHIBITS RECEIVED	361
4. BRIEFINGS/INSPECTIONS	365
5. COMMISSIONER'S OF TAXATION 1910 TO 1993	367
6. BRANCH OFFICES OF THE AUSTRALIAN TAXATION OFFICE ..	369
7. CHARTER OF THE NATIONAL TAX LIAISON GROUP	371
8. CHARTER OF THE COMMISSIONER'S ADVISORY PANEL	373
9. TAXATION RULING TR93/30 - PUBLIC RULING	375
10. A PRIVATE RULING	385
11. TAXATION DETERMINATION TD93/94	391
12. TAXPAYER'S CHARTER	393
Minority Report of Senator B K Bishop	395

LIST OF FIGURES

	Page
Figure 3.1 Australian Taxation Office Organisation Structure As at 1 June 1993	32
Figure 6.1 The Process for the Preparation of Rulings	100

LIST OF TABLES

Table 7.1 Planned Reductions in the Running Costs Budget of the Australian Taxation Office Stemming From Modernisation 1993-94 to 1995-96	145
Table 7.2 Modernisation Funding as at 1991-92	146
Table 8.1 Salary and ASL 1991-92 to 1996-97	151
Table 8.2 Estimated and Actual Administrative Expenditure - Australian Taxation Office 1988-89 to 1992-93	166
Table 8.3 Effect of the 1.25% Efficiency Dividend on Australian Taxation Office's Approved Staffing Level (ASL) 1993-94 to 1996-97	174
Table 8.4 Estimated Salary Reduction in the Australian Taxation Office resulting from the 1.25% Efficiency Dividend 1993-94 to 1996-97 (based on projected average salary rates)	175
Table 8.5 Estimated Revenue Returns from Compliance Strategy 1994-95 and 1995-96	183
Table 8.6 Large Business Segment - Estimates of Increased Revenue	184
Table 8.7 Small Business Segment - Estimates of Increased Revenue	185

Table 8.8	Non-Business Individuals - Estimates of Increased Revenue	185
Table 9.1	Revenue Collection by the Australian Taxation Office 1960-61 to 1989-90	196
Table 9.2	Real Percentage Change in Revenue Collection 1983-84 to 1992-93	197
Table 9.3	Cost of Collections as a Percentage of Revenue Collected 1960-61 to 1989-90	198
Table 9.4	Change in Actual Collections over Budget Forecasts 1980-81 to 1992-93	200
Table 9.5	Unpaid Income Tax at 30 June, 1988-89 to 1992-93	212
Table 9.6	Percentage of Tax Unpaid to Total Tax for Individuals, Companies and Trusts 1988-89 to 1992-93	212
Table 9.7	Tax Debt Written Off under Section 70C of the <i>Audit Act 1901</i> , 1981-82 to 1992-93	214
Table 9.8	Tax and Duty Foregone 1987-88 and 1992-93	224
Table 10.1	Inquiry Statistics July 1991 - April 1992	227
Table 11.1	Market Segmentation	249
Table 11.2	Costs and Benefits of Audit 1989-90 to 1991-92	282
Table 11.3	Audits of Members of Parliament (State and Federal) for the Three Year Period up to 31 October 1992	288
Table 14.1	Taxation Workload of the Administrative Appeals Tribunal 1986-87 to 1992-93	328
Table 14.2	Workload of Federal Court in Taxation Related Matters 1987-88 to 1992-93 - Cases Filed or Transferred from State Supreme Courts	333
Table 14.3	Workload of Federal Court in Taxation Related Matters 1987-88 to 1992-93	333

EXECUTIVE SUMMARY

The Report

1. When the Federal Land Tax Department was first created in 1910, it had a very limited, though important, responsibility in supporting the collection of revenue for the Commonwealth. Today's Australian Taxation Office (ATO) carries on that responsibility through the annual collection of more than \$70 billion of revenue. Every Australian citizen is affected by the manner in which the ATO performs its role and, significantly, the ATO's administration of the taxation laws impacts directly on the efficiency of the Australian economy.

2. The Report of the Committee's Inquiry into the Australian Taxation Office (ATO) is divided into three Parts. Part 1 deals with issues concerning the ATO's operations and organisation. A history of the ATO is included in this Part. The daily interaction of the ATO with taxpayers and the functioning of the ATO are evaluated in Part 2. Practical issues for taxpayers in their dealings with the taxation system are raised in Part 3.

The Income Tax Assessment Act 1936

3. The Inquiry into the ATO was concerned with the administration of the taxation system of Australia. Questions of the tax mix and policy were not considered. However, from the earliest moment the Committee recognised that the efficiency of taxation administration was related directly to the efficiency of Australia's principal taxation Act, the *Income Tax Assessment Act 1936* (the Act). As possibly the most important piece of economic legislation in Australia, the Committee found the Act was in desperate need of a comprehensive overhaul. Not only has the Act developed into a complex and incomprehensible mass of convoluted, legalistic and pedantic provisions but, most importantly, the uncertainty of its meaning acts as a positive detriment to the welfare of Australia.

4. The Committee clearly determined that a bipartisan will must be found to ensure the Act is completely redrafted and framed for modern Australia. The language must be simplified and the operation of the Act's provisions constructed in a manner which supports taxpayers in their obligations. Significant resources for this task will need to be provided immediately and the task should be allocated to a specific all-party task force drawn from experts in every domain of Australian life.

5. While the Act's redraft is an economic and social imperative, the Committee considered that a commitment to cease adding administratively burdensome provisions to the Act was equally important. To this end the Committee considered the Parliament's role was paramount. Information on the cost impact of new legislation needs to be made available to the Government and the Parliament for evaluation and consideration. In addition the formulation of taxation legislation needs to be reformed to explicitly acknowledge the interrelationship of policy and administration.

Management of the Australian Taxation Office

6. In attempting to administer the Act, the ATO utilises the skills and resources of approximately 18 000 staff and expends in excess of \$1 billion annually. The Committee has evaluated the organisational framework of the ATO and concluded that after 80 years the framework needs to be updated and refashioned. To allow the ATO to meet the challenges of an international economy and to broaden the management expertise at the most senior levels of the organisation, the Committee has determined that the ATO should be established as an autonomous Australian Taxation Commission, dedicated to the administration of the taxation system.

7. Moreover, the Committee has established that the accountability links between the Parliament and the Commissioner of Taxation need to be transparent. While continuing to preserve the Commissioner's independent administration of taxpayer cases, the Committee concluded that the management of the ATO needs to be structured in a manner which parallels the accountability paths existing in other government organisations.

Self Assessment

8. The Committee has evaluated the system of self assessment. The importance of taxpayer compliance with, and understanding of, the obligations imposed by the Act has been starkly exposed by introduction of the self assessment system. The Committee recognised the administrative efficiencies of self assessment for the ATO. However, the Committee sees an urgent need for a review of the responsibilities and practical implications of the system for taxpayers and their agents. Increased support to assist taxpayers to satisfy their obligations is also required.

Rulings

9. The Committee acknowledges the critical importance of the dissemination of information in a self assessment environment. The imbalance of powers between taxpayers is considered by the Committee to require a fundamental re-evaluation of the roles of the administrator and the legislator. The Committee affirms its belief that only the Parliament has the power to make law. In no circumstance should an administrator have the capacity to impose upon citizens obligations which cannot be supported clearly in law. The Committee acknowledged that a consequence of the costs of access to judicial interpretation was the effective transfer to the Commissioner of the power to define the law.

10. The role of the Commissioner's Rulings was extensively evaluated by the Committee, which formed the view that the Commissioner needs to be more accountable for the Rulings. In addition, the fundamental status of Rulings as simply the Commissioner's view of the law needs to be affirmed. The Committee found that the imposition of administrative penalties for taxpayers who failed to follow Rulings was inconsistent with the standing of Rulings as advice and therefore inappropriate.

The Modernisation Program

11. The Committee evaluated the progress to date of the ATO's modernisation program. The Committee recognised that significant technological programs for the collection of tax had been developed by the end of the first four years of the ATO's ten year \$1 billion program. Nevertheless the Committee expresses concern at the technical planning of the modernisation project and, in particular, the program's priorities.

Resources

12. The Committee expresses genuine concern at the financial position of the ATO. The consequences of recent borrowings and resource transfers were considered to have deeply disturbing implications for the ATO's long term efficiency. The Committee considers that a combination of factors stemming from the economic recession, when combined with the limitations in the Modernisation Agreements with the Public Sector Union and the Department of Finance, have meant that the ATO has had to sacrifice its current operational efficiency and future restructuring so as to be able to afford to pay current staff. The Committee considers these matters have been treated in a paternalistic fashion which has placed in doubt the capacity of the ATO to effectively embrace the potential of modernisation.

Decentralisation

13. Decentralisation of the ATO's branch office structure has been an essential component of the ATO's modernisation program. The Committee appreciated the object of decentralisation but is concerned about the capacity of the ATO to afford the additional property space it has acquired. Restricted by funding agreements, the ATO must commence resource planning to anticipate reductions in its property funding. The priority of accommodation for staff will thus need to be contrasted with the service provided to taxpayers. The Committee determines the latter must come first.

Auditing

14. With self assessment, audit has become a critical component in the ATO's ability to collect revenue. The public face of the ATO is most commonly seen through the activity of the staff of the ATO's Audit Group. The Committee has found that auditors exercise powers which are unparalleled and not conducive to independent, professional and objective auditing as it is commonly understood. The Committee found that professional, technical auditing would be facilitated best by separating the roles of information collection, analysis and report from the decision making process associated with audit assessment.

15. In addition, the Committee believes it is critical that the ATO modify the processes of making taxation assessments such that the decisions relayed to taxpayers are fully supportable and justified in writing. This will require the ATO to institute a formal system of internal review within the decision making process so that the ATO can justify and explain its final decisions to taxpayers.

Small Taxation Claims Tribunal

16. Taxpayer access to independent review of the decisions of the ATO was considered by the Committee. It was established by the Committee that the court system does not provide a satisfactory protection against administrative maladministration and the cost of accessing the judicial system frustrates taxpayers seeking redress through the courts. The Committee determines that, with a minimal outlay, a significant number of taxpayer complaints could be managed by a low cost small taxation claims tribunal.

Taxation Ombudsman

17. The Committee recognised that there was a need to provide a sufficiently resourced technical expert in taxation within the Commonwealth Ombudsman's Office. To support the work of the Taxation Ombudsman, the Committee considers there is a need to link the independent scrutiny of the Ombudsman with internal investigation and review functions within the ATO. The Committee found that this objective could be facilitated by requiring that the staff of the ATO's Problem Resolution Units work directly to the Taxation Ombudsman.

Charter of Rights

18. The Committee has noted that there is an imbalance between taxpayers and the ATO in relation to their formally stated rights and obligations. The Act, together with other legislation, provides the ATO with a clear and powerful operational basis. The Committee found that taxpayers need to be provided with an equivalent statement which formally sets out those standards which they should expect from the ATO and its staff.

Culpability Penalties

19. The determination of a person's intentions generally requires evaluation of a mixture of objective evidence and subjective perceptions. When penal sanctions are attached to these determinations the Committee has concluded that the process of making them should be strictly limited to persons technically specialised in the drawing of inferences. Generally this will require that the decisions be made by courts. The Committee found that the ATO utilises culpability penalties in substitution for prosecutions; that is, rather than referring a matter to a court, ATO staff draw the necessary inferences themselves. The Committee considers this situation untenable - it should be abandoned in favour of administrative penalties for objective offences only. Issues of culpability should be settled by the courts, not administrators.

Privilege

20. The Committee considered the operation of the doctrine of legal professional privilege and has concluded that this issue should be referred to a specialist investigatory body to determine whether its continued operation is conducive to the efficient operation of the taxation system. The Committee also believes the essential characteristic of the doctrine needs to be protected by the imposition of sanctions against those who would abuse it.

21. In addition the Committee has considered several issues concerning the relationship between the ATO and taxpayers. In particular it has evaluated the quality and accessibility of ATO advice and assistance. The Committee considers the ATO still has some way to go in providing a sufficiently high quality service to both taxpayers and their agents to enable them to satisfy their obligations according to law.

22. The Committee has examined the efficiency of the ATO's revenue estimation and collection procedures. The Committee considers the ATO needs to do significantly more to improve the accuracy and timeliness of its revenue estimates. Debt collection procedures and the writing off of bad debts were particularly important considerations for the Committee.

23. Other issues considered by the Committee included the treatment of taxpayer hardship, review procedures, the quality of correspondence produced by the ATO and the training requirements of ATO staff.

RECOMMENDATIONS

The Committee has made a number of recommendations which are set out below, cross-referenced to their location in the text.

The Committee recommends that:

Administrative Structures

1. The Australian Taxation Office be established by statute under its own Charter as the Australian Taxation Commission. (paragraph 3.46)
2. The general power of administration of taxation Acts be vested in the Commission's Chief Executive Officer who shall be known as the Chief Commissioner of Taxation. (paragraph 3.46)
3. The Australian Taxation Commission be established with a one line budget appropriation. (paragraph 3.52)
4. The Chief Commissioner of Taxation be able to recruit and employ staff on terms and conditions determined by the Chief Commissioner with the agreement of the Treasurer. (paragraph 3.52)
5. The Australian Taxation Commission report on its resources to the Parliament in accordance with the current practice of the Australian Taxation Office and be fully available for on-going scrutiny by the Parliament. (paragraph 3.52)
6. In order to reinforce the independence of the Chief Commissioner, so much of the taxation laws of Australia be amended as would allow the Minister responsible for taxation matters to issue directions to the Chief Commissioner of Taxation concerning the manner in which the Chief Commissioner exercises the general powers of administration conferred on the Chief Commissioner by the various taxation laws. (paragraph 3.80)

7. The relevant Minister responsible for taxation matters be required to table before both Houses of the Parliament within five sitting days of having issued a direction to the Chief Commissioner of Taxation in respect of the exercise of the general powers of administration, a copy of the relevant direction. (paragraph 3.80)
8. Until the relevant Minister has satisfied the requirement to table the issued direction, the said direction shall have no effect and the Chief Commissioner of Taxation shall not be required to comply with the said direction. (paragraph 3.80)
9. The power to issue directions not apply in respect of the application of taxation laws to individual taxpayers. (paragraph 3.80)
10. The *Public Service Act 1922* be amended to require the Chief Commissioner of Taxation to report annually to the Minister on the operations of the Australian Taxation Commission. (paragraph 3.86)
11. The Chief Commissioner be required to comply with so much of the guidelines for annual departmental reports as would not involve breaches of Section 16 of the *Income Tax Assessment Act 1936*. (paragraph 3.86)
12. The functions of the current Deputy Commissioners of Taxation be couched in terms of branch or regional establishment management. (paragraph 3.100)
13. The title of the current Deputy Commissioners of Taxation be amended to more accurately reflect their revised role. (paragraph 3.100)
14. The Australian Taxation Office require all complaints against individual case auditors be put in writing. (paragraph 3.119)
15. The role of advisory committees be formalised and strengthened within an Australian Taxation Commission. (paragraph 3.131)
16. Advisory committees be structured so as to play a positive role in the context of a revised administrative framework. (paragraph 3.131)

17. Specific advisory committees be established as necessary, to interact with Commissioners of the Australian Taxation Commission on identifiable projects. (paragraph 3.131)
18. The names of members of advisory bodies be published together with the names of the organisations they represent in the Annual Report of the Australian Taxation Commission. (paragraph 3.131)

Self Assessment

19. The further extension of the self assessment system be delayed pending the development of a comprehensive supporting legislative framework. (paragraph 4.44)
20. The Australian Taxation Office develop and make publicly available appropriate information for taxpayers on their obligations under a self assessment system. (paragraph 4.44)

Legislative Framework

21. The Government introduce legislation to amend Section 128F of the *Income Tax Assessment Act 1936* to clarify its meaning and application. (paragraph 5.19)
22. The Government establish a broadly based task force to redraft the *Income Tax Assessment Act 1936*. (paragraph 5.38)
23. The Government commit sufficient resources to the task force as will allow it to complete a priority simplification redraft within two years and the full simplification of the Act within five years. (paragraph 5.38)
24. Where legislation is foreshadowed in an administrative announcement, the Commissioner of Taxation be required to release significant details of the proposed legislation and the Government commit itself to the introduction of enabling legislation within six months of the announcement or before the end of the relevant taxation year, which ever is the sooner. (paragraph 5.51)

25. A Taxation Administration Brief prepared by the Australian Taxation Office be submitted by the Treasurer to the Cabinet setting out the administration implications of each policy proposal involving amendments to any Act under the administration of the Commissioner of Taxation. (paragraph 5.58)
26. All future taxation legislation be supported by a Taxation Impact Statement which details the impact on taxpayers of the legislation, including the total compliance cost and the extent to which simplification objectives have been achieved. (paragraph 5.67)
27. Officers of the Office of Parliamentary Counsel responsible for the drafting of taxation legislation be located in the Australian Taxation Office for the purpose of drafting taxation legislation. (paragraph 5.72)

Rulings

28. The Commissioner of Taxation acknowledge in a public Ruling the existence of alternative interpretations of the law to that which has been taken in the Ruling. (paragraph 6.26)
29. Where an acknowledgment of alternative interpretations of the law is included in a public Ruling, the Commissioner of Taxation outline the basis of those alternative views. (paragraph 6.26)
30. Where the Commissioner of Taxation is provided with arguments evidencing a serious doubt as to the validity of an interpretation in a Ruling, the Commissioner refrain from making a public Ruling pending the clarification of the law. (paragraph 6.26)
31. All public Rulings be subject to formal approval by the proposed Australian Taxation Commission prior to their release. (paragraph 6.31)
32. For the purposes of Section 14ZAAJ of the *Taxation Administration Act 1953*, a public Ruling be defined to have been published only when notice of the Ruling is published in the Commonwealth Gazette. (paragraph 6.36)

33. A notice of publication for the purposes of the gazettal of public Rulings include the reference number and subject heading of the Ruling, together with a brief general description of the Ruling's effect, along the lines of the current head note to public Rulings. (paragraph 6.36)
34. The Australian Taxation Office make available, on subscription, access to the information database on which the Commissioner's public Rulings are maintained. (paragraph 6.36)
35. Full versions of all public Rulings issued by the Commissioner of Taxation be tabled in the Parliament within five sitting days of notice of their publication being included in the Commonwealth Gazette. (paragraph 6.66)
36. All private Rulings be maintained upon a computer database and made readily accessible to the public in a format which does not identify the individual taxpayer. (paragraph 6.70)
37. The *Income Tax Assessment Act 1936* be amended to remove the imposition of an administrative penalty for a taxpayer who assesses their taxation liability in a manner which is not consistent with a private Ruling that has been issued to them, provided the taxpayer indicates in their annual tax return that their private Ruling has not been followed. (paragraph 6.72)
38. Income tax return forms be amended to allow taxpayers to indicate where they have not followed a private Ruling. (paragraph 6.72)
39. The Australian Taxation Office have the discretion to charge for the provision of private Rulings on significant hypothetical issues where under Section 14ZAN of the *Taxation Administration Act 1953*, the Commissioner of Taxation would otherwise determine that insufficient resources existed to provide the requested Ruling. (paragraph 6.77)
40. Culpability penalties not apply to taxpayers who fail in their assessment to follow a Determination issued by the Australian Taxation Office. (paragraph 6.80)
41. There be an annual Taxation Clarification and Technical Corrections Bill to facilitate the simplification and technical correction of the *Income Tax Assessment Act 1936* and associated legislation. (paragraph 6.84)

42. The Australian Taxation Office review its issued private and public Rulings and Determinations for the purposes of determining the continued validity of all Rulings. (paragraph 6.98)
43. All private and public Rulings and Determinations of the Australian Taxation Office be consolidated and referenced in a form which facilitates easy access by taxpayers. (paragraph 6.98)

Modernisation

44. The relationship between tax agents and the Australian Taxation Office be clarified, so that no agency relationship can be construed to exist between the tax agent and the Australian Taxation Office. (paragraph 7.30)
45. The Australian Taxation Office review the legislative framework supporting all initiatives arising out of both modernisation and self assessment. (paragraph 7.30)
46. The Australian Taxation Office establish, in consultation with the accounting profession and the computer software industry, an Electronic Lodgement Service audit and support unit for the purposes of testing and certifying software produced for use on the Electronic Lodgement Service. (paragraph 7.30)
47. Electronic Lodgement Service generated returns indicate whether the return was processed using a certified computer software program. (paragraph 7.30)
48. The Australian Taxation Office seek to develop, as part of its business systems, facilities for the access of tax agents and others to a number of databases of the Australian Taxation Office, in particular the client listings database and the legal information system database. (paragraph 7.30)
49. Where a taxpayer lodges a return through an Electronic Lodgement Service terminal, the Australian Taxation Office pay the requisite service fee in recognition of the economic benefit it derives. (paragraph 7.30)

50. The Australian Taxation Office monitor and evaluate the relative use of TaxLAN facilities throughout its organisational Groups and develop programs to facilitate the productive utilisation of TaxLAN's functionality. (paragraph 7.41)
51. The Australian Taxation Office increase the priority within the modernisation system of the migration of information onto the National Office Management Administration System. (paragraph 7.50)
52. Information on the National Office Management Administration System be fully utilised for human resource management reporting and planning. (paragraph 7.50)
53. The specialist cells be provided with sufficient resources to enable them to have full time members and adequate technical and administrative support to provide both a service to officers within the Australian Taxation Office and a point of direct access for taxpayers. (paragraph 7.71)
54. The Auditor-General conduct an evaluation of the effect of the Public Sector Union Modernisation Agreement on the efficiency of the Australian Taxation Office. (paragraph 7.78)
55. The Australian Taxation Office prepare estimates and targets for revenue gains, cost savings and performance standards expected from the implementation of the Collection Systems Modernisation project. (paragraph 7.91)
56. The Australian Taxation Office report progress and performance against targets for the Collection Systems Modernisation project in the Commissioner's Annual Report. (paragraph 7.91)

Resources

57. The Auditor-General evaluate and report on the efficiency and effectiveness of the program of excess staff transfers between the Australian Taxation Office and other departments. (paragraph 8.24)

58. The Australian Taxation Office introduce a coordinated national program of training, counselling and support for officers interacting regularly with taxpayers for the purpose of improving the interpersonal skills of those officers. (paragraph 8.33)
59. The Australian Taxation Office, through the utilisation of officers responsible for legislative developments, investigate and implement a method of informing and training technical officers and staff, who directly interrelate with taxpayers, about the progress of legislative developments. (paragraph 8.44)
60. The Australian Taxation Office investigate methods to utilise retired officers and retired private sector practitioners in the training of staff. (paragraph 8.53)
61. The Australian Taxation Office and relevant staff unions cease all negotiations for increases in staff salaries based on increased revenue returns to the Commonwealth. (paragraph 8.60)
62. The Government amend its guidelines on the payment of productivity based wage increases to remove any possibility of revenue returns being used as a measure of productivity. (paragraph 8.60)
63. The Joint Select Committee on Certain Family Law Issues review the allocation to and expenditure of administrative expenses by the Child Support Agency. (paragraph 8.68)
64. The Department of Finance conduct a comprehensive review and evaluation of the base administrative expenditure requirements of the Australian Taxation Office. (paragraph 8.79)
65. The Australian Taxation Office commence an immediate review of its property program to ensure that the threshold space allocations required by the Modernisation Funding Agreement can be achieved within three years. (paragraph 8.87)

66. The Department of Finance, in association with the Australian Taxation Office and the Australian Bureau of Statistics, review the workload formula and develop a new formula that seeks to model the marginal needs of the Australian Taxation Office in such a way that allows for medium term planning and management priority decision making. (paragraph 8.99)
67. The Australian Taxation Office prepare estimates of possible revenue gains relating to all systems redevelopment proposals which pertain to modernisation developments, including changes to administrative practices and procedures and advise the Government of those estimates. (paragraph 8.109)
68. The Australian Taxation Office develop a means for measuring the revenue impact of the Income Tax Compliance/Enforcement Strategy and report to the Parliament on the Strategy's outcomes in the Commissioner's 1994-95 and 1995-96 Annual Reports. (paragraph 8.131)
69. The Australian Taxation Office include in the Commissioner's Annual Report, staffing information in respect of the Income Tax Compliance/Enforcement Strategy and, in particular, report information on the number of staff positions created and the number of positions filled by applicants from outside the Office. (paragraph 8.135)
70. The Australian Taxation Office and the Department of Finance establish a reciprocal program of officer interchange. (paragraph 8.144)
71. The Department of Finance allocate sufficient resources to allow officers, who have regular dealings with resource issues affecting the Australian Taxation Office, to visit and inspect the operations of an Australian Taxation Office branch office at least once a year. (paragraph 8.148)

Revenue Collection

72. The Australian Taxation Office set for itself a performance target of reducing the cost of collection to less than one percent of annual revenue collected by 1995-96. (paragraph 9.17)

73. The Australian Taxation Office review its current revenue forecasting models in consultation with the Treasury, Australian Bureau of Statistics and other forecasting agencies. (paragraph 9.27)
74. The Australian Taxation Office seek to develop an on-going modelling capacity which can provide Government with predictions of monthly revenue collections and an early warning mechanism in the event of significant changes to the forecast pattern of revenue collection. (paragraph 9.27)
75. The Australian Taxation Office review its procedures for random examination checking of assessments and notices produced by the Automatic Data Dispatch system for the purpose of ensuring incorrect assessments and notices are not issued. (paragraph 9.37)
76. Where an assessment or notice is issued which contains an error produced by either human or computer failure and the taxpayer draws the existence of this error to the attention of the Australian Taxation Office, the taxpayer receive either a discount on the issued debt notice or a bonus on the tax refund. (paragraph 9.37)
77. The Government institute amendments to the operation of the Provisional Tax System for the purposes of establishing a simplified administrative system for the calculation of provisional tax. (paragraph 9.49)
78. The Australian Taxation Office determine a comprehensive national policy for debt collection based on the economic cost of recovery. (paragraph 9.72)
79. The Australian Taxation Office ensure a consistent application of policy in the writing-off of tax debts in the Revenue Collection Group. (paragraph 9.72)
80. The Australian Taxation Office introduce a streamlined system for the write-off of bad debts based solely on an evaluation of the potential for recovery. (paragraph 9.72)
81. The Australian Taxation Office develop facilities for monitoring the management of taxpayer hardship cases on a national basis. (paragraph 9.101)

82. The Australian Taxation Office report statistics on hardship cases in the Commissioner's Annual Report. (paragraph 9.101)

Taxpayers Assistance

83. The Australian Taxation Office introduce, as a standard throughout their branch networks, 008 telephone numbers for taxpayer contact and information. (paragraph 10.18)
84. The Australian Taxation Office publicly commit itself to follow all advice provided in writing to taxpayers. (paragraph 10.23)
85. Where taxpayers seek oral advice from the Australian Taxation Office, they be advised of their right to request confirmation of that advice in writing. (paragraph 10.23)
86. Where a taxpayer requests written confirmation of oral advice from the Australian Taxation Office, the taxpayer receive a written response no later than ten working days after the oral advice has been provided. (paragraph 10.23)
87. The Australian Taxation Office adopt as a corporate standard the obligation to assess taxpayers in accordance with information contained in publications released by the Office. (paragraph 10.28)
88. All publications released by the Australian Taxation Office contain a statement detailing the right of taxpayers to rely upon the information contained in the publications. (paragraph 10.28)
89. The Australian Taxation Office review the strategic use of TaxPack and develop the concept as a primary document, indicating available alternative sources of information in relation to specific industries, taxpayers and provisions of the *Income Tax Assessment Act 1936*. (paragraph 10.32)

90. The Australian Taxation Office introduce a formal mechanism for the determination of cases where contradictory advice has been received by a taxpayer from two or more branch offices. Such a procedure should incorporate a formal decision making process and a method for the dissemination of the final advice to all Australian Taxation Office branch offices. (paragraph 10.44)
91. The Australian Taxation Office review the quality and quantity of resources devoted to providing direct assistance to tax professionals. (paragraph 10.52)

Auditing

92. Auditors in the Australian Taxation Office be briefed on the reasons for a case being selected for audit, the briefings to stress the need to improve voluntary compliance. (paragraph 11.35)
93. All audit staff in the Australian Taxation Office undergo extensive training in financial reporting analysis. (paragraph 11.38)
94. All audit staff in the Australian Taxation Office be trained in accounting requirements, standard financial auditing techniques, methodologies and systems. (paragraph 11.38)
95. The Australian Taxation Office ensure external input is sought in the provision of financial and accounting training for its auditors, such training to have a commercial rather than academic orientation. (paragraph 11.38)
96. The Australian Taxation Office amend its tax return forms to enable taxpayers to indicate why significant variations in their affairs generally or in a particular area had occurred in an income year. (paragraph 11.43)
97. Corporate taxpayers attach to their annual taxation returns basic financial report information including, where appropriate, full, audited financial statements. (paragraph 11.47)

98. The Australian Taxation Office review its information sources to determine whether the taxation return provides the most efficient means of gathering information. (paragraph 11.51)
99. The Australian Taxation Office review its methods for checking trust returns to ensure that the information disclosed in trust returns is checked against all beneficiary returns. (paragraph 11.51)
100. The Australian Taxation Office establish a database of generic lists of taxpayers gathered pursuant to Sections 263 and 264 of the *Income Tax Assessment Act 1936*. (paragraph 11.84)
101. The Australian Taxation Office's database of generic lists of taxpayers be security protected so that access is only possible where a case requires it. (paragraph 11.84)
102. The existence of the Australian Taxation Office's database of generic lists of taxpayers be publicly disclosed in the Commissioner's Annual Report. (paragraph 11.84)
103. Section 263 of the *Income Tax Assessment Act 1936* be amended to require that the Australian Taxation Office show just cause before being granted a warrant by an appropriate judicial official to access or enter the private property of a taxpayer without permission. (paragraph 11.87)
104. The Australian Taxation Office install facilities in all branch offices to allow taxpayer interviews to be electronically recorded and that all taxpayers be automatically given a copy of that interview, within seven days at no cost. (paragraph 11.91)
105. The Australian Taxation Office purchase equipment to allow for recorded interviews to be conducted at taxpayers' premises. (paragraph 11.91)
106. The Australian Taxation Office cease the practice of having taxpayers sign statements or transcripts of interviews. (paragraph 11.91)

107. The Australian Taxation Office discuss with a taxpayer prior to a formal audit interview the obligation of the taxpayer to answer questions according to law and, in all cases, notify the taxpayer of his/her right to representation. (paragraph 11.91)
108. The Legislative Services Group in the Australian Taxation Office be reconstituted to form a Legal and Legislative Service Group within the Office. (paragraph 11.100)
109. Staff of the Advising Branch of the Taxpayer Assistance Group involved in statutory interpretation be aligned functionally with the Legal and Legislative Service Group. (paragraph 11.100)
110. The Australian Taxation Office introduce a formal system of quality controlled internal decision making review which identifies formal mechanisms for taxpayer participation in decision making and specifies the appropriate level of review and supervision for decision making. (paragraph 11.109)
111. The Australian Taxation Office commit itself to providing decisions to taxpayers which are final and supportable in the first instance. (paragraph 11.109)
112. The Australian Taxation Office reallocate the resources of the Appeals and Review Group to the performance of internal review within the on-going decision making processes of the Australian Taxation Office. (paragraph 11.111)
113. *Section 170 of the Income Tax Assessment Act 1936* be amended to allow adjustments to the assessment of a taxpayer's tax liability that involve a year of income four years prior to the year in which the audit commences, provided the taxpayer was notified of the review of that assessment within four years of the assessment having been originally made. (paragraph 11.116)
114. So much of the law be amended as would allow a system of deficiency notices to be introduced for taxpayers who would be made technically insolvent by the issue of an amended taxation assessment. (paragraph 11.141)

115. The Australian Taxation Office separate the functional roles of the Taxpayer Audit Group by establishing a unit independent of the Taxpayer Audit Group with responsibility for making decisions regarding amended assessments. (paragraph 11.150)
116. The role of auditors within the Australian Taxation Office's Taxpayer Audit Group be clarified and limited to the investigation and preparation of reports on taxpayers. (paragraph 11.150)
117. The Taxpayer Audit Group in the Australian Taxation Office be headed by a senior professional auditor responsible for the technical development of audit skills within the Office and the maintenance of quality standards within the Taxpayer Audit Group. (paragraph 11.150)
118. In the preparation of taxation audit reports, officers of the Taxpayer Audit Group in the Australian Taxation Office obtain all legal and interpretation advice from officers in the Office's Legal and Legislative Service Group. (paragraph 11.150)
119. The group made responsible for determining audit cases in the Australian Taxation Office establish a priority program for litigating cases where the application of provisions of the *Income Tax Assessment Act 1936* is unclear. (paragraph 11.155)
120. Such a litigation program be conducted at no cost and with no penalty to the test case taxpayer. (paragraph 11.155)
121. All audit settlement negotiations be conducted in the presence of no less than three officers of the Australian Taxation Office, with one of the negotiating officers being the auditor responsible for the taxpayer's case. (paragraph 11.159)
122. All audit settlement negotiations be audio recorded and a copy of the tape provided to the taxpayer within seven days of the discussion. (paragraph 11.159)

123. The Australian Taxation Office review its administrative arrangements for the supervision, monitoring and auditing of non-resident beneficiary trusts and determine as a matter of priority administrative and/or policy mechanisms to better control abuses of interest withholding tax. (paragraph 11.170)
124. As a matter of priority, the Australian Taxation Office seek to obtain double taxation treaties with those countries which are significant destinations for distributions from Australian trusts. (paragraph 11.170)
125. The Australian Taxation Office conduct a survey of skills within its Taxpayer Audit Group for the purposes of establishing a register of currently available skills and to enable the development of appropriate training responses. (paragraph 11.175)
126. The Commissioner of Taxation publish each year in the Annual Report the broad statistical details of the number of Restricted Access Status Taxpayers subject to audit, without identifying any taxpayer group. (paragraph 11.188)

Enforcement and Penalties

127. The *Income Tax Assessment Act 1936* be amended to remove the capacity of officers of the Australian Taxation Office to impose administrative culpability penalties. (paragraph 12.31)
128. If culpability penalties are retained in the law, they be determined in all instances by a legally qualified officer of the Australian Taxation Office who is independent of the Taxpayer Audit Group. (paragraph 12.31)
129. The Australian Taxation Office review its guidelines and instructions in respect of prosecutions to ensure all references to the issue of potential or actual publicity are removed. (paragraph 12.39)
130. Sub-section 83E(2) of the *Taxation Administration Act 1953* be amended to remove the right of the Commissioner of Taxation to re-impose a culpability penalty in the circumstances where a prosecution is withdrawn. (paragraph 12.46)

Taxpayers' Charter

131. The Government consider establishing a Taxpayers' Charter based on a review of the various models available. (paragraph 13.28)
132. A statutory position of Commonwealth Taxation Ombudsman be created within the current Commonwealth Ombudsman's Office. (paragraph 13.42)
133. Resources be provided to the Commonwealth Taxation Ombudsman to allow the Ombudsman to adequately investigate all complaints. (paragraph 13.42)
134. The role of the Problem Resolution Units in the Australian Taxation Office be amended such that the staff of those Units work directly to a Commonwealth Taxation Ombudsman. (paragraph 13.42)
135. Reports by the Commonwealth Taxation Ombudsman on taxpayer complaints be provided both to the taxpayer and the Commissioner of Taxation. (paragraph 13.42)
136. A report on the activities of the Commonwealth Taxation Ombudsman be incorporated in the Annual Report to Parliament of the Commonwealth Ombudsman. (paragraph 13.42)
137. The Attorney-General refer the question of the operation and impact of the doctrine of legal professional privilege, as it applies to the administration of the taxation system, to the Australian Law Reform Commission for evaluation, review and report. (paragraph 13.53)
138. The Australian Law Reform Commission in evaluating the operation of the doctrine of legal professional privilege give consideration to the impact of the doctrine on the treatment of advice on taxation matters passing between taxpayers, lawyers and other professional advisers, vis a vis, the Australian Taxation Office. (paragraph 13.53)

139. The Australian Law Reform Commission, as part of a reference into legal professional privilege, investigate and make recommendations on the administrative mechanisms for handling claims for privilege and the need to provide a sanction for persons who make unreasonable claims. (paragraph 13.56)

Avenues of Review

140. The current taxation law of Australia be amended to allow the establishment of a Small Taxation Claims Tribunal within the registry of the Administrative Appeals Tribunal. (paragraph 14.30)
141. The relevant taxation laws of Australia be amended as to allow the establishment of a procedure to permit taxpayers to lodge objections against, or seek review of, decisions of the Australian Taxation Office before a Small Taxation Claims Tribunal. (paragraph 14.30)
142. Where the amount of tax in dispute with the Australian Taxation Office is less than \$5 000, a taxpayer be able to elect to have their objections or reviews of decisions heard by the Small Taxation Claims Tribunal. (paragraph 14.30)
143. A \$50 non-refundable fee be required to be lodged by taxpayers seeking review of decisions of the Australian Taxation Office in the Small Taxation Claims Tribunal. (paragraph 14.30)
144. Any decision of a Small Taxation Claims Tribunal be final and non-appealable. (paragraph 14.30)
145. Where a taxpayer intends to take a matter before the Small Taxation Claims Tribunal, the Australian Taxation Office have the option to refer the matter to the Federal Court of Australia provided all the taxpayer's costs, including legal representation, are met by the Australian Taxation Office. (paragraph 14.30)

146. Sections 14ZZE and 14ZZJ of the *Taxation Administration Act 1953* be amended so as to establish the presumption that hearings before the Administrative Appeals Tribunal in taxation matters are held in public unless the taxpayer elects to hold the hearing in private. (paragraph 14.35)

147. The Government encourage the reporting of taxation cases from the Administrative Appeals Tribunal under a single reporting series. (paragraph 14.35)

148. In all cases where the Australian Taxation Office is unsuccessful at any stage of litigation and a decision is made to appeal the relevant decision, the Office fully fund the taxpayer's expenses in defending the case. (paragraph 14.49)

ABBREVIATIONS

AAT	Administrative Appeals Tribunal
ABS	Australian Bureau of Statistics
ADD	Automated Document Dispatch
ADP	Automatic Data Processing
AGPS	Australian Government Publishing Service
AIMS	Automated Income Matching Systems
ANAO	Australian National Audit Office
APS	Australian Public Service
ASL	Average Staffing Level
ATO	Australian Taxation Office
ATAX	Australian Taxation Studies Program
ATRF	Australian Tax Research Foundation
CAP	Commissioner's Advisory Panel
CATA	Computer-Assisted Tax Auditing
CCA	Compliance Cost Assessments
CSM	Collection Systems Modernisation
CTC	Chief Tax Counsel
DPP	Director of Public Prosecutions
EDR	Exposure Draft Ruling
EFT	Electronic Funds Transfer
ELS	Electronic Lodgement Service
FBT	Fringe Benefits Tax
FCU(TOB)	Federated Clerks Union (Taxation Officers' Branch)
FMIS	Financial Management Information System
FTE	Full Time Equivalent
HECS	Higher Education Contribution Scheme
HRM	Human Resource Management
IPSS	Integrated Payment and Service System
IRiS	Information and Research Services
IRS	United States Internal Revenue Service
IT	Information Technology
ITAA	<i>Income Tax Assessment Act 1936</i>
IWT	Interest Withholding Tax
LCP	Large Case Audit Program
LSG	Legislative Service Group
MIN	Management in the Nineties
NOMAD	National Office Management Administration System
OECD	Organisation for Economic Co-operation and Development
OPC	Office of Parliamentary Counsel
PAYE	Pay-As-You-Earn
PBA	Project Based Audit
PCEK REPORT	Pappas, Carter, Evans and Koop Report
POE	Property Operating Expenses
PPS	Prescribed Payments System

PRU	Problem Resolution Unit
PSU	Public Sector Union
RAST	Restricted Access Status Taxpayer
RFT	Request for Tender
SES	Senior Executive Service
SOG	Senior Officer Grade (Grades: A, B and C)
TaxLAN	Tax Local Area Network
TFN	Tax File Number
TIA	Taxation Institute of Australia
TLG	Tax Liaison Group
TPC	Trade Practices Commission
US	The United States of America

PART 1 - PRINCIPAL ISSUES

- CHAPTER 1** **Introduction**
- CHAPTER 2** **Historical Background**
- CHAPTER 3** **Administrative Structures**
- CHAPTER 4** **Self Assessment**
- CHAPTER 5** **Legislative Framework**
- CHAPTER 6** **Rulings**
- CHAPTER 7** **Modernisation**
- CHAPTER 8** **Resources**

Chapter 1

INTRODUCTION

- . Background
- . Terms of Reference
- . Conduct of the Inquiry
- . The Evidence
- . Structure of the Report

Background

1.1 Many aspects of the Australian Taxation Office (ATO) are regularly reviewed by the Parliament. Examples of this scrutiny include Senate Estimates Committees and examinations of relevant reports of the Auditor-General by various committees, of both Houses of Parliament. In recent years significant investigations have been undertaken by the House of Representatives Standing Committee on Finance and Public Administration, the Senate Standing Committee on Finance and Public Administration and the Joint Committee of Public Accounts, which in 1987 tabled a report on the ATO's major computer redevelopment proposal.

1.2 Cognisant of this diverse parliamentary scrutiny the Committee determined in November 1991 it would conduct a wide ranging review of the administration and operation of the ATO. The decision was taken in light of a number of significant changes which had occurred in the administration of taxation over recent years. These included the move to a self assessment system, the expansion of taxpayer audits as an enforcement arm of administration and the public revelation of administrative problems within the ATO.

1.3 In determining to conduct the Inquiry, the Committee was particularly concerned to evaluate the impact of ATO operations on average Australian taxpayers. The Committee considered it to be imperative that the balance between taxpayers' rights and the ATO's obligations, as the Commonwealth's principal revenue collector, be clearly defined and maintained.

Terms of Reference

1.4 The terms of reference for the Inquiry were agreed to on 6 November 1991 and were:

To inquire into and report on the administrative procedures adopted by the Australian Taxation Office (ATO) in the collection of taxation revenues pursuant to the *Income Tax Assessment Act 1936-1991*, with particular reference to:

- . the administrative and operational structures of the ATO and the application of common standards of practice across Australia;
- . the efficiency and effectiveness of self assessment;
- . the authority and application of taxation Rulings;
- . the use of information technology within the ATO; and
- . the resources of the ATO and their allocation.

Conduct of the Inquiry

1.5 In November 1991 the Seventeenth Joint Committee of Public Accounts determined to conduct a wide ranging inquiry into the administrative procedures adopted by the ATO in the collection of taxation revenues.¹ The Inquiry was advertised nationally in major newspapers on the weekend of 8-9 February 1992 and invitations to make submissions were issued to relevant community and professional groups and individuals. During 1992, the Seventeenth Committee made inspections of three ATO offices and conducted 13 public hearings in Canberra and selected State capitals.

1.6 On 22 October 1992, the Treasurer announced that it was the intention of the Government to appoint the Commissioner of Taxation, Mr Trevor Boucher, as Ambassador to the OECD.² Mr Boucher was the chief

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1. The Committee had previously conducted a detailed examination of aspects of the Taxation Office during its 1987 Inquiry into the Computer Redevelopment Proposal. Discussion of the Committee's 1987 Inquiry is contained in Chapter 7 of this Report.
 2. OECD - Organisation for Economic Cooperation and Development.

architect behind the massive program of changes in the ATO during the last decade. The Committee acknowledges the significant contribution made by Mr Boucher during his lengthy and distinguished service with the ATO and wishes him well in his new post.

1.7 Mr Michael Carmody was appointed to succeed Mr Boucher as Commissioner Designate, from 21 November 1992 until 22 January 1993 when he was confirmed in his position as the new Commissioner of Taxation.

1.8 On 13 May 1993, following the Federal Election in March, the newly constituted Eighteenth Committee, under the Chairmanship of Mr Les Scott, MP, resolved to resume the Inquiry into the Australian Taxation Office.

1.9 The current Committee conducted a further two public hearings in Canberra in June 1993 and subsequently met privately with the Commissioner on more than one occasion to discuss a number of matters.

The Evidence

1.10 During the course of the Inquiry, in excess of 120 submissions were received, amounting to over 5 000 pages of evidence. Details of these submissions are listed at Appendix 1. A further 1 600 pages of evidence was taken during the fifteen public hearings conducted during 1992 and 1993. Details of the public hearings and witnesses who appeared are set out at Appendix 2. Details of the exhibits tendered by witnesses are listed at Appendix 3. The Committee also made inspections of the ATO's premises in Parramatta, Canberra and Adelaide. Details of these inspections are listed at Appendix 4.

1.11 In receiving this large body of evidence the Committee reaffirms the right of individuals to provide evidence to the Committee without fear of victimisation or recrimination of any sort. Any attempt to interfere with a person giving evidence to the Committee in this way will be regarded with great seriousness by the Committee. This Committee declares its intention to exercise its powers under the *Public Accounts Committee Act 1951* to receive all the evidence it requires to conduct its inquiries to the fullest extent possible and its preparedness to go to the highest authority to protect all those who give evidence to it.

Structure of the Report

1.12 The Report is divided into three parts. Part 1 - Principal Issues (Chapters 1 - 8) - focuses on the terms of reference, with Chapter 2 providing the important history of the ATO. Part 2 - ATO Operations and Taxpayers (Chapters 9 - 12) - deals with issues relating to the operations of the ATO and taxpayers while Part 3 - Taxpayer and the ATO (Chapters 13 and 14) - concerns issues which relate specifically to taxpayers.

Chapter 2

HISTORICAL BACKGROUND

- . Introduction
- . 1910 - 1960
- . 1960 - 1980
- . 1980 - 1992

Introduction

2.1 The history of an organisation is important in any examination of its current operation and future direction. This is particularly so in the case of the Australian Taxation Office (ATO). This chapter traces the history of taxation in Australia from the 1910 antecedent of the ATO, the Federal Land Tax Department, through to present day developments in the ATO.

2.2 The history of taxation in Australia provides a useful background to an appreciation of the culture of the ATO and shows that the chief objective of taxation of all forms has been the raising of revenue. Redistribution of income and reduction of wealth inequality can be seen, particularly in the case of income taxes, to have been latter day objectives of government policy.¹ The Committee noted that the structure of Australia's income tax system also provides incentives to certain forms of economic behaviour. For example, the system has been used to provide incentives in areas as diverse as encouraging research and development, encouraging investments in Australian films and encouraging the making of gifts to various charitable organisations.

1910 - 1960

2.3 On 1 July 1910 the Federal Land Tax Department commenced operations, even though the legislation which imposed the tax and that which provided for its collection, the *Land Tax Act 1910* and the *Land Tax Assessment Act 1910*, did not receive the Governor-General's assent until 16 November 1910 and

1. Ross S, Burgess P, *Income Tax - 'A Critical Analysis'*, Law Book Company 1991, p. 4.

17 November 1910 respectively. Under these laws the tax payable for the first year was due after the hour of noon on 30 June 1910.²

2.4 The first Federal Land Tax Commissioner, Mr G A McKay was appointed on 11 November 1910 and a month later six Deputy Commissioners, one for each State, were also appointed. Major G Steward, Deputy Commissioner of Taxation for Victoria obtained a transfer from that position shortly after his appointment. By June 1912 no replacement had been appointed and the Commissioner, who was based in Melbourne, undertook the necessary duties for Victoria. The position of Deputy Commissioner for Victoria was re-established in 1915. A list of the Commissioners of Taxation from 1910-1993 is included at Appendix 5. The national administration of the Federal Land Tax Department was initially carried out from a central office in Melbourne. It was not until 1933 that Taxation Office staff moved to the Head Office in Canberra.

2.5 In those early years, a large number of temporary staff were utilised as the permanent staff requirements of the Land Tax Department were undetermined. Recruitment and staff retention were a constant problem for the Land Tax Department as evidenced by the Department's early experience in which it reported that it was:

... difficult to secure, from the ordinary avenues of appointment to the Commonwealth Service, the class of assistance necessary to carry out the more important work of the Department.³

2.6 The administrative and organisational arrangements for the Land Tax Department were established at a conference of the Deputy Commissioners and the Commissioner between 12 December and 22 December 1910. It was determined at that time that the administration needed to be decentralised. In his first Annual Report to the then Treasurer, The Right Honourable Andrew Fisher, PC, MP, Commissioner McKay reported:

It was at once realised that any attempt to centralise the administration of details would fail, as the distances of the State offices from the Central office were so great that delays and inconvenience would inevitably occur.⁴

2. Commissioner of Land Tax, *First Annual Report*, Government Printer for the State of Victoria, p. 3.

3. *ibid.*

4. *ibid.*, p. 7.

2.7 As a consequence it was determined that the Head Office would determine and define the policy of the Department under the law with that policy being adjusted, as necessary, for the exigencies of the States. The Deputy Commissioners, under delegated authority, would exercise local control within the limits of the defined policy. On this arrangement, Commissioner McKay reported:

This, with a provision for keeping in touch with every phase of the work in its progress and with a clearly defined system of office control and management, has enabled the Department to accomplish its work up to the present with a minimum of friction and an expedition as great as the complicated nature of the law would admit.⁵

2.8 Over the following years, the ability of the Federal Land Tax Department to secure a permanent staffing establishment and employ suitably qualified staff was delayed by the imposition of additional Commonwealth levies. In response to the need for additional revenue caused by World War I, the Commonwealth introduced an estate duty (1914), an income tax and war-time profit tax (1915) and finally an entertainments tax (1916). The 1915 income tax had an exemption of £150, and a progressive scale ranging from 2.5% to 25%, the latter on incomes over £7 600. This tax was in addition to State income taxes although the payment of State income taxes were allowed as a deduction from Commonwealth income tax.⁶ With the increased breadth of the revenue base, the Federal Land Tax Department became known as the Commonwealth Taxation Office in 1918.

2.9 The need to administer these new taxes during the war further exacerbated the staffing position which had become critical as a result of enlistments for military duty. In part this resource problem was accommodated by the employment of female officers and temporary male staff. The employment of female staff was so unusual that it induced the Commissioner of the day to write, in restrained praise, that female labour was 'used extensively on routine work, and has proved satisfactory.'⁷ On 1 November 1917 an Assistant Commissioner of Taxation was appointed to assist the Commissioner in the discharge of the general administration powers.⁸

5. *ibid.*

6. Ross, Burgess, *op. cit.*, p. 4.

7. Commissioner of Taxation, *Sixth Annual Report*, Government Printer for the State of Victoria, 1917, p. 4.

8. *ibid.*, p. 29.

2.10 In 1911-1912 the total staff of the Taxation Office numbered 105 and this rose to 1 565 in 1919-1920. As is still the case today, the retention of highly qualified staff was a major problem for the Taxation Office. This was especially so between the two World Wars. Following World War I, many of the most capable taxation officers resigned and entered private practice where they were reported to have, 'quickly established practices which were several times more lucrative than their positions in the Department.'⁹

2.11 In 1922, a Royal Commission on Federal Economies examined the operation of taxation in Australia, particularly the overlap of State and Commonwealth taxes and the administration of taxation. The recommendations of that Commission covered subjects as broad as the operation and interaction of company taxes in the Commonwealth and States and the need for proper accommodation for Taxation Office staff.¹⁰ The latter remains a current issue.

2.12 With concurrent income tax administrations being run by the States and Commonwealth there was clearly an opportunity to rationalise administration. Following World War I, avenues were examined for consolidating revenue collection throughout the Commonwealth. From 1 July 1921, the Commonwealth undertook to collect both its own taxes and the whole of the taxes imposed by the State of Western Australia.¹¹

2.13 Protracted negotiations then followed between the other States and the Commonwealth to establish a single authority responsible for the collection of taxes. As a consequence of these discussions, in late 1923 and early 1924, the income tax branches of the Taxation Departments of the Commonwealth and all States except Western Australia, were combined. All Commonwealth and State income taxes were thus assessed and collected by the Commissioner of Taxation of the relevant State. Commonwealth staff engaged in assessing and collecting income tax were merged with the State employees, and the officers thus transferred became State officers, subject to the provisions of the respective State Public Service Acts and Regulations. However, it was not until 1936 that each State Taxation Commissioner was appointed as a Deputy Federal Commissioner of Taxation for Commonwealth purposes.¹² A consequence of these arrangements was the

9. Commissioner of Taxation, *Seventh Annual Report*, Government Printer for the State of Victoria, 1921, p. 7.

10. Royal Commission on Taxation, *Third Report*, Commonwealth Government Printer, Canberra, 1922.

11. Commissioner of Taxation, *Thirty-Ninth Annual Report*, Commonwealth Government Printer, 1960, p. 18.

12. Commissioner of Taxation, *Eighteenth Report*, Commonwealth Government Printer, 1936, p. 5.

reduction in the number of Commonwealth Taxation Office staff from around 1 900 to under 700.¹³

2.14 While this system of State-based administration worked relatively well, there were significant differences in the various State income tax laws and State officials tended towards an individualistic approach in interpreting both the State and Commonwealth Acts. It was thus possible for a business deduction to be disallowed under one Act but allowed under another.¹⁴

2.15 Such inconsistencies resulted in a further Royal Commission in 1930, which produced a proposal for a uniform tax assessment Act, although uniform rates were not settled to allow for State differentials. The consequential *Income Tax Assessment Act 1936* remains the basis of the imposition of a national income tax, though it has grown in size far beyond that ever envisaged in 1936.

2.16 Administration of the uniform Act continued to be performed by all States, except Western Australia, until 1942 when the staff of the State income tax offices temporarily transferred to the Commonwealth. At that time it was anticipated that those transfers would last for the duration of the war and twelve months thereafter.¹⁵ At the outbreak of World War II new taxes were introduced which included:

- . a pay-roll tax;
- . a war-time (company) tax;
- . a gold tax; and
- . gift duties.

2.17 Furthermore the scope and incidence of other taxes, such as income tax, were expanded as the Government determined that the war effort would be financed, to the largest extent possible, from current revenue rather than through borrowings. This resulted in greatly increased workloads for the Taxation Office at a time when enlistments to the military services were resulting in losses of permanent staff. Once again extensive utilisation of female staff was necessary and

13. *ibid.*

14. Ross, Burgess, *op. cit.*, p. 5.

15. Commissioner of Taxation, *Thirty-Ninth Annual Report*, Commonwealth Government Printer, 1960, p. 19.

by 30 June 1945 the percentage of female officers in the Commonwealth Taxation Office had reached 57.1%.¹⁶

2.18 The nature of taxation administration irrevocably altered during the war years. In 1939-40 income tax collection represented 47% of the total revenue for the Commonwealth. By 1944-45, that percentage had risen to 78%. Total income tax collections in that financial year amounted to £211.8 million compared to £16.4 million in 1939-40.¹⁷ As well, the Commonwealth introduced in 1944-45 the Pay-As-You-Earn (PAYE) system of tax collection by which employers made weekly deductions of tax from the employee's wage on behalf of the Taxation Office. The highest marginal rate in 1944-45 was a staggering 75%. Rates on property income were even higher. This contrasted to the rates applying in the States before the War. For example, in Victoria, a single taxpayer's personal exertion income of £3 000 was taxed at a rate of 3.8%.¹⁸

2.19 All temporary staff transferred from the States were appointed permanently to the Commonwealth Service from 1 July 1946 following a decision to continue uniform taxation. In each State, except Western Australia and Victoria, there were thus two Commonwealth Taxation Offices - one administering income tax and the other the remaining Commonwealth levies. The Victorian situation was quite complex. The Central Office administered income tax for certain taxpayers with interstate interests and the remaining Commonwealth taxes except for entertainments tax. The former State Office administered income tax for residents of Victoria and entertainments tax.¹⁹

2.20 It was not until the 1950s that the two taxation offices in the remaining States were amalgamated.²⁰ The history of the Commonwealth Taxation Office in this period was characterised by large workloads and ever increasing revenue collections. For example, income tax revenue collected from individuals increased in 1951-52 over the previous financial year by a massive 93%, principally as a result of increased inflation stemming from a commodities boom associated with the Korean War and tax rate rises. The burden of income taxation was principally borne by those on above average earnings with the Commissioner estimating in 1951 that 10% of taxpayers earned 37.7% of taxable income and paid 88.7% of total individual income tax.²¹

16. *ibid.*

17. Ross, Burgess, *op. cit.*, p. 5.

18. *ibid.*

19. *ibid.*

20. Hobart (1955), Brisbane (1956), Adelaide (1957) and Sydney (1958).

21. Ross, Burgess, *op. cit.*, p. 6.

1960 - 1980

2.21 By 1960 the total staff of the Taxation Office numbered approximately 7 500 and annually handled:

- . 4 900 000 income tax returns;
- . 500 000 sales tax returns;
- . 300 000 pay-roll tax returns;
- . 17 000 estate duty returns; and
- . 9 000 gift duty returns.²²

2.22 Accommodation problems for the Taxation Office remained in the 1960s. A general shortage of office accommodation following World War II exacerbated the problem. The Commissioner noted in 1960, 'Progress is being made but any schemes to improve accommodation are necessarily comprehensive and long-term in nature.'²³

2.23 As a result of the passing of the *Taxation Administration Act 1959*, a second office of Second Commissioner of Taxation was established. This change to the administrative organisation was considered necessary as a result of an increased workload and an increase in the number of taxation Acts administered by the Commonwealth Taxation Office.²⁴

2.24 Also, in the early 1960s automated data processing was recognised as having the potential to provide efficiencies, through the processing of large quantities of data. An evaluation group was established in 1960-61 to assess, 'whether automatic data processing equipment would result in increased efficiency and worthwhile savings in administrative costs.'²⁵

22. Commissioner of Taxation, *Thirty-Ninth Annual Report*, Commonwealth Government Printer, 1960, p. 19.

23. *ibid.*

24. *ibid.*, p. 16.

25. Commissioner of Taxation, *Fortieth Annual Report*, Commonwealth Government Printer, 1961, p. 8.

2.25 It was not until 1965, that certain work involving instalment deductions and other minor projects in the South Australian branch office was carried out by computer. The success of these trials was sufficient to warrant an expansion of computer technology into other fields and other States. By 1968, the automatic data processing system was said to provide:

... for the calculation of tax, preparation of assessment notices and refund cheques, the verification of the amount of credit to be allowed for instalment deductions and provisional tax, the preparation of accounting and other internal control documents and the tabulation of statistical information. In addition, the computer was used to account for payments received from employers in ... Queensland, South Australia, Western Australia and Tasmania and for the preparation of final notices to persons in those States and in Victoria who had failed to lodge income tax returns.²⁶

2.26 While computers were providing a facility to rapidly process data and perform repetitive processing functions, an associated consequence was the Taxation Office's need to employ staff to program the automated system and enter data. Together with a general increase in the volume of work and additional tasks associated with the change to decimal currency in 1966, the Commonwealth Taxation Office's staffing figure reached over 10 000 in July 1966. By the end of the following year, the staffing figure was consistently above that level.

2.27 In 1969-70, significant changes were introduced to the organisational and administrative structures. A need was identified for additional executive resources in the Head Office and a re-organisation of the Division Structure of the Head Office was completed. Increased emphasis was placed on policy development and research as a result of the expanding complexity and coverage of taxation law. State branches were allocated additional Assistant Deputy Commissioners to bring more positive direction to the work of State branches and better service to taxpayers needing assistance in discussing major problems with senior officers.²⁷

2.28 New methods of income tax investigations and company income tax assessment were adopted at the operational level. The use of small, coordinated

26. Commissioner of Taxation, *Forty-Eighth Annual Report*, Commonwealth Government Printer, 1969, p. 4.

27. Commissioner of Taxation, *Forty-Ninth Annual Report*, Commonwealth Government Printer, 1970, p. 3.

groups under close supervision was encouraged for investigations. Of specific interest, given future events, was the decision to place:

Particular emphasis ... on developing more sophisticated techniques for selecting cases for investigation, so that taxpayers who have complied with their responsibilities under the law will not lightly be troubled, and so that any necessary checks will be carried out with a minimum of inconvenience to them.²⁸

Thus, perhaps, were sown the seeds of modern methods of self assessment, case selection and auditing.

2.29 From the start of the 1970-71 financial year, the historical oddity of two Commonwealth Taxation Offices in Melbourne was abandoned. This move was a response to the realities of commercial life and the efficiencies which automatic data processing had produced. State offices were now capable of processing returns of taxpayers who earned income across Australia and, as a result, a processing function within the Central Office was redundant.

2.30 With the transfer of some work back to the States in line with shifts in the division of taxation responsibilities stemming from the uniform, national *taxation of income*, the Commonwealth Taxation Office entered the 1970s with a national organisation structure, national policy focus, increasing workloads, continuing accommodation problems, a primitive yet evolving computer system and increasing staff numbers. It is clear now, with the benefit of hindsight, that while the organisation was not ideally placed to manage the upheavals in taxation practices that were about to unfold in the 1970s, the seeds of change that were to characterise the Taxation Office in later years had already been planted.

2.31 The development of the Taxation Office in the 1970s can fairly be characterised as a microcosm of Australian society during those years. Concentration, indeed enthusiasm, for the development and expansion of computer technology dominated the focus of the Taxation Office in the early years of the decade. During 1972-73 the Commonwealth Taxation Office became the Australian Taxation Office (ATO) and plans were implemented for the introduction of a fully automated taxation processing system based on a very large central computer complex in Canberra. For an outlay, estimated in 1973 to be around \$2.4 million, a

28. *ibid.*

Cyber 72 computer system was purchased.²⁹ In addition, the ATO collaborated in the development of an advanced mini-computer system tailored to the special processing needs of the Office. The purpose of this development was to provide data entry facilities in the branch offices. While direct access to the central computer was possible, the majority of bulk data processing was performed in the Head Office through data transfer by magnetic tapes.

2.32 Throughout the 1970s, the ATO extended its use of computer technology across programs, functions and offices. Issues such as the efficiency of processing, the refinement and creation of new programs and the development of on-line facilities became imperatives. Moreover, computer technology allowed the creation of new administrative procedures and job designs, including the development of a new technique called 'taxpayer audit', in 1975-76.

2.33 As technology was embraced by the ATO, other issues prevalent in society at large came to be recognised as significant. Subjects of importance included:

- . work measurement, productivity and performance appraisal;
- . management training;
- . career development;
- . word processing;
- . ergonomics; and
- . work environments.

2.34 All the seemingly permanent problems of the ATO continued during the 1970s. While the ATO expanded its regional office structure and new branch offices were established as part of a decentralisation plan, severe accommodation problems continued to frustrate improvements in working conditions.

2.35 The ATO also developed a new culture and language of its own. Principally as a result of an increased social awareness of the importance of taxation, or perhaps despite such an increased awareness, the ATO developed a new central, organisational division responsible for the management of issues concerning taxpayer compliance.

29. Commissioner of Taxation, *Fifty-Second Annual Report*, Commonwealth Government Printer, 1973, p. 6.

2.36 By the middle of the decade, it had become increasingly apparent that taxation schemes were being marketed in society with the purpose of evading taxation obligations. A literalist High Court, in a string of celebrated cases, ruled in favour of these schemes, thus encouraging their further promotion. These schemes had the consequence of producing a severe haemorrhaging of Commonwealth revenues and added very significantly to the volume and complexity of administrative work.³⁰

2.37 The birth and subsequent flourishing of contrived taxation arrangements, severely curtailed the ATO's administrative functioning. The impact and complexity of the schemes required a massive diversion of staff resources across all organisational groups. In a sense, while the ATO was continually acting to plug holes in the revenue bucket, the scheme promoters simply moved on to develop more convoluted and secretive arrangements which pierced the bucket's lining.

2.38 Frustration, and more than a small measure of anger, pervaded the ATO, not least because promoters of taxation schemes made use, perhaps even abused, every possible administrative avenue including the appeal and objection procedures. Indeed, the ATO was faced with the situation in which the evader gained a benefit from the delay in assessment, even if their arrangement was ultimately ruled illegal.

2.39 Throughout this period staff numbers remained remarkably constant despite the massive increases in workload. Fiscal controls over spending, brought about by general economic conditions, meant that individual productivity, rather than staff numbers, had to increase to meet the unprecedented rise in workloads. Over the decade, the cost of revenue collection as a percentage of total revenue fell from 0.992% in 1970-71, to 0.889% in 1980-81.³¹

1980 - 1992

2.40 In 1980-81 a comprehensive review of the administrative structures of the ATO's Head Office was conducted. As a result of substantial increases in workload volumes, a major reorganisation of the Head Office was effected. Also in that year an upgrade of the central computer facility was approved. This upgrade was considered necessary to provide for additional capacity. In reality, the central

30. Commissioner of Taxation, *Fifty-Sixth Annual Report*, Commonwealth Government Printer, 1977, p. 5.

31. Commissioner of Taxation, *Fifty-Eighth Annual Report*, Commonwealth Government Printer, 1971, p. 64; and the Commissioner of Taxation, *Sixtieth Annual Report*, Commonwealth Government Printer, 1981, p. 65.

computer facility was already beginning to demonstrate severe weaknesses due to functional and operational stress. A system which was initially intended to merely be a data processing facility was now being called upon to undertake a multitude of tasks and processes.

2.41 The computer system of the ATO was not alone in suffering a high degree of stress as a result of the scheme promoters of the 1970s. Clearly the social and political environment confronting the ATO at the turn of the decade was unprecedented. Never before had the administration been so vitally challenged. Economical, efficient, responsive and intelligent structures for taxation administration needed to be considered.

2.42 With political support and a significant legislative commitment, the ATO was able to evaluate its goals and respond more capably to the Government's agenda. Between 1978 and 1983 at least 34 separate Acts were passed by the Parliament amending the substantive provisions of the *Income Tax Assessment Act 1936*. Amongst the most notable changes during this period were:

- . the introduction of numerous amendments to counter evasion schemes;
- . the introduction of Part IVA (anti-avoidance); and
- . the establishment of Division 13 (international profit shifting).

2.43 In addition, the *Crimes (Taxation Offences) Act 1980* was passed. This Act, established a number of criminal offences relating to the fraudulent evasion of income tax and sales tax by stripping companies or trusts of their capacity to pay tax. Following the change of government in 1983, further legislative changes significantly impacted on the ATO's administration.

2.44 It was only as the evasion schemes were being mopped up that the full extent of the administrative problem became apparent. With the new Government came a rush of new administrative and economic imperatives. In responding to these, the ATO was at first constrained by the need to process the workloads of past years. In his first annual report, Commissioner Boucher stated, 'The legacy that remains continues to affect our ability to achieve all that we would like to achieve'.³²

32. Commissioner of Taxation, *Sixty-Third Annual Report*, AGPS, 1984, p. 6.

2.45 It would be reasonable to suggest that the attitude, even culture, of the ATO which emerged from the evasion scheme years was vastly different from that which existed before. While the ATO was at first defensive about its role during those years, noting that critics needed to remember that choices had to be made in administration,³³ step by step it became determined to again embrace the Australian community. The tone of the Commissioner's Reports to the Treasurer during the 1980s reflected this attitude shift. So too did the move towards self assessment. The significance of the Commissioner's 1984 statement, 'Most taxpayers comply voluntarily'³⁴, cannot be underestimated.

2.46 By 1984-85 staff numbers had reached 15 000. As the Government introduced numerous legislative changes, staff resources continued to expand. Nevertheless, pressures in the areas of information technology, accommodation, skill levels, assessment objections and reviews remained.

2.47 During 1980-81 an extensive review of assessing policies and practices within the ATO was carried out to ensure that the standards which assessors were required to refer to, in dealing with doubtful or questionable claims, were both realistic and defensible.³⁵ At the same time, greater effort was devoted to resolving disputes at the earliest possible stage. These administrative adjustments were considered necessary to reduce the pressures on resources then being experienced as a result of the growth in disputation of assessments through the objection and appeal provisions. These changes had some immediate impact on the number of objections raised. However, there continued to be a sizeable growth in objections. Much of that growth was attributable, in the ATO's view to, 'taxpayers attempting to delay or avoid payment of tax by involvement in "scheme" activities.'³⁶

2.48 The early years of the 1980s witnessed significant changes for the ATO both in administration and organisation. Upgrading of both the ATO's computer facilities and collection systems were accorded a high priority. Nevertheless, the general economic conditions also required greater efficiencies from the Office. Functions were rationalised where possible. The positions of Australian Taxation Representative in London and Washington were withdrawn during 1980-81. It should be recognised that while the ATO was engaged in significant introspection, this was conducted in the context of a general Public Service review.

33. *ibid.*

34. *ibid.*, p. 6.

35. Commissioner of Taxation, *Sixtieth Annual Report*, Commonwealth Government Printer, 1981, p. 4.

36. *ibid.*

2.49 Following the release of reports by the Royal Commission on the Activities of the Federated Ship Painters and Dockers Union and the Inspectors Appointed to Investigate the Particular Affairs of Navillus Pty Ltd and 922 Other Companies, the ATO felt it necessary to publicly defend its administration of the tax laws as they pertained to dangerous and criminal elements of the community.³⁷ The need for this defence highlighted the tension and stress which the ATO had been placed under by the operation of schemes of evasion. Some critics of the ATO at this time argued that insufficient effort had been given to enforcing the anti-avoidance provisions as they then existed in s. 260 of the *Income Tax Assessment Act 1936*.

2.50 By 1982-83, revenue collections by the ATO exceeded \$30 000 million.³⁸ Given the resource pressures experienced by the ATO it was perhaps inevitable that staff disputations would begin to occur with greater frequency. The ATO responded administratively in 1982-83 by establishing an Industrial Relations Section. Also in that year legislation was passed which was to have profound administrative implications for the ATO. On 1 December 1982, the *Freedom of Information Act 1982* came into effect. While it was initially considered to have most significance in the area of personal records and access to documents, the ATO was conscious of the Act's implications for the, 'method of publishing and disseminating decisions relevant to the interpretation and application of taxation laws.'³⁹ The future significance of Rulings may not then have been apparent.

2.51 Tax avoidance statistics prepared by the ATO in 1982-83 indicated the enormity of the administrative and resource effort imposed on the ATO by the promotion of avoidance schemes. By 15 October 1983, 48 891 objections had been lodged by 29 444 taxpayers against the disallowance of their claims. The tax which had been sought to be avoided totalled \$1 298.5 million. Many of the cases in dispute dated back six to seven years.⁴⁰

2.52 While the blatant scheme era was nearing its end, the implications for taxation administration generally, and the ATO specifically, were yet to be fully revealed. The use of retrospective legislation, 'legislation by press release', the establishment of special prosecutors, the importance of international transactions and the breakdown in trust between the community and the ATO were all features of this period which were to have ramifications for the future.

37. Commissioner of Taxation, *Sixty-First Annual Report*, Commonwealth Government Printer, 1982, p. 4.

38. Commissioner of Taxation, *Sixty-Second Annual Report*, Commonwealth Government Printer, 1983, p. 4.

39. *ibid.*, p. 7.

40. *ibid.*, p. 9.

2.53 In 1983-84 the new Commissioner wrote in his first annual report of practicality in administration:

Even in the best times, tax administration is not a perfect art. The ideal, the desirable, may have to give way to what it is that is practicable. And the judgement about what is practicable must be made, in prevailing circumstances, on the basis of the always - limited resources (be they human, material or legal) that are available to deal with the whole range of matters demanding attention.⁴¹

2.54 The need to review assessment capabilities and the processing of income tax returns was identified as part of an on-going process of improvement. Indeed review of all operations and structures was given a much higher priority in the ATO's program than at any time previously.

2.55 The program of decentralisation which commenced in 1975, was expedited during the 1980s. Throughout the decade, the ATO opened no less than seven branch offices. A full list of the ATO's branch offices and their opening dates is included at Appendix 6. The acquisition of appropriate accommodation was given even greater impetus by the modernisation program which adopted decentralisation as a core ingredient.

2.56 Much of the history of the ATO between 1983 and 1991 is included in the ATO's submission to the Inquiry.⁴² The following summary, drawn from the ATO's submission and the annual reports of the Commissioner of Taxation, highlights a number of the significant changes.

1983-84

- . structural re-organisation - Head Office Directorates created
- . tax return forms reviewed and simplified
- . use of computer prepared returns considered

41. Commissioner of Taxation, *Sixty-Third Annual Report*, AGPS, 1984, p. 6.

42. Evidence, vol. 4, pp. S670-S1013.

- . target audit coverage for non-salary and wage earners of 2% by 1992 established
- . taxation collection systems established or modified for legislative changes including the introduction of Medicare and the Prescribed Payments System
- . serious computer inadequacies identified and strategies developed to remedy deficiencies
- . Director of Public Prosecutions established
- . Audit and Investigations areas reorganised into a Compliance Branch

1984-85

- . decision taken to move to self-assessment systems, following in-depth review
- . bulk settlement of some scheme arrangements encouraged
- . changes made to penalty provisions to introduce economic reality in penalty levels
- . practice of naming significant defaulters abandoned
- . Corporate Plan developed and released
- . Public Information Unit established
- . Industrial Democracy, Equal Employment Opportunity and Occupational Health and Safety programs introduced
- . Tax Liaison Groups established

1985-86

- . tax collections reached \$45 billion
- . Australian National Audit Office efficiency audits prepared
- . number of objections to assessments reduced by 64%
- . number of appeals on hand reduced by 51%

- . over 750 pages of legislation produced together with over 1 200 pages of explanatory material
- . large write-off of amounts of tax associated with company strip assessments increased the irrecoverable tax written off to \$91.5 million
- . program budgeting introduced
- . staff attrition rates reached 15%
- . ADP strategic plan developed and implemented
- . Taxation Board of Review ceased to operate from 1 July 1986 - responsibility transferred to the Taxation Appeals Division of the Administrative Appeals Tribunal

1986-87

- . National Desk Audit program commenced
- . ATO Management Board created
- . Program Management Performance Review conducted by Dr Ron Cullen
- . Office Structures Review recommendations implemented
- . modernisation proposal endorsed by Cabinet
- . ATO Computer re-equipment and redevelopment proposal examined by Joint Committee of Public Accounts
- . Taxpayer Service Group established
- . irrecoverable tax written off increased to \$163 million
- . Fringe Benefits Tax introduced
- . employment related expenses and car and travel expenses where expenses exceed \$300 in total, require substantiation

1987-88

- . revenue collections reached \$60 billion
- . pilot project for electronic lodgement of returns trialled in Adelaide
- . Child Support Agency opened
- . ATO Audit Section restructured into three areas: Complex; Business; and Primary Audit
- . Problem Resolution Program commenced
- . Community Based Tax Assistance program trialled in Newcastle
- . Quarterly Provisional Tax System introduced
- . lodgement amnesty commenced
- . House of Representatives Standing Committee on Finance and Public Administration Report, *A Taxing Review*, tabled
- . Tax Administration Skills Program introduced
- . Graduate Development Program, *Taxation Officer Development Program* established
- . company tax imputation commenced
- . irrecoverable tax written off equalled \$651.5 million
- . Score System introduced to Audit
- . Senate Standing Committee on Legal and Constitutional Affairs Report, *Report on the System of Taxation Rulings*, tabled

1988-89

- . Tax File Number legislation introduced
- . Commissioner's Advisory Panel established
- . Large Case Audit program commenced

- . ATO Bursary Scheme introduced to encourage staff to continue their education
- . Integrated Human Resource Management Plan developed
- . House of Representatives Standing Committee on Finance and Public Administration tabled three reports - *A Tale of Three Cities* (November 1988), *Shifting the Tax Burden ?* (November 1988), and *Taxpayers or Tax Players ?* (May 1989)
- . Senate Standing Committee on Finance and Public Administration Report, *The Administration of the Tax File Numbers System*, tabled

1989-90

- . Tax Pack implemented
- . Electronic Lodgement Service launched
- . the McKinsey Report on the ATO's relationship with Tax Agents and large companies released
- . simplification review announced
- . Higher Education Contribution Scheme implemented

1990-91

- . self assessment arrangements introduced for companies and superannuation funds
- . Foreign Source Income and Resource Rent Tax legislation implemented
- . Returns Processing Counter Service implemented
- . Modernisation Agreement with the Public Sector Union signed
- . data matching introduced

2.57 By the start of the 1991-92 financial year, the ATO was actively pursuing its goal of modernisation. Many pilot projects had been commenced and planning advanced for the introduction of major changes to structures and systems. In particular, integrated client based teams had been created to allow one-stop-shopping for the provision of services to taxpayers. Throughout the period of the Inquiry the ATO continued to decentralise its branch office network, such that at the time of reporting the ATO was operating out of 24 branch offices. Two further offices are due to be opened in January 1994.⁴³ As at October 1993 the ATO employed approximately 17 700 full time staff. Full details on the ATO's resources are contained in Chapter 8.

43. Evidence, vol. 22, p. S5333.

Chapter 3

ADMINISTRATIVE STRUCTURES

- . Current Administrative Structures
- . Efficiency of the Current Administration and Organisational Structures
- . Senior Management Structure - Proposals for Change
- . International Comparison
- . Revised Management Structure
- . Second Commissioners
- . National Program Managers
- . Deputy Commissioners
- . External Advice

3.1 It is clear from the history of the Australian Taxation Office (ATO) that it has progressed from a relatively small organisation with limited responsibilities to a relatively large bureaucracy with numerous social, political and economic objectives. Nevertheless, the basic administrative structure of the ATO has changed very little over the last 80 years.

3.2 In evaluating the administrative structures the Committee was cognisant of various propositions and proposals for changes to the senior administrative structures of the ATO which were being debated within the wider community. The Committee considered that any proposal for change should be evaluated on the basis of its contribution to the efficiency and effectiveness of taxation administration.

3.3 Consequently, the Committee considered and evaluated the current ATO structures against three broad subject categories:

- . the extent to which the administrative and organisational structures facilitate the performance of the duties of revenue collection and other functions required of the ATO by the Government and the Parliament;
- . the extent to which the administrative structure contributes to, and enhances the independence of, the holder of the general power of administration; and

the degree of accountability provided by the administrative and organisational structures.

Current Administrative Structures

3.4 The current administrative structures of the ATO were described in a chapter of the ATO's submission to the Inquiry.¹ Briefly summarised, general responsibility for the administration of both the taxation laws and the operation of the ATO is vested in the Commissioner of Taxation. The Commissioner's power of general administration derives from specific provisions in individual taxation Acts.² The Commissioner is currently assisted in the task of administration by three Second Commissioners.

3.5 Technically the ATO is not a legal entity. By law only the Office of the Commissioner of Taxation and Second Commissioners exist and, as described in Chapter 2, the ATO has evolved as the bureaucracy to support the Commissioner.

Program Structure

3.6 For the purposes of reporting to the Parliament, the ATO is included in the program structure of the Commonwealth Treasury Portfolio. Under this program the ATO has identified four principal sub-programs:

- . Income Tax;
- . Sales Tax;
- . Corporate Support; and
- . Child Support.³

3.7 The Committee considered all four sub-programs during its Inquiry although most attention was devoted to the Income Tax and Corporate Support sub-programs. The Sales Tax sub-program was only evaluated in terms of its relationship within the overall organisational structure because it was considered sufficiently analogous in its objectives and operational composition to the Income

1. Evidence, vol. 4, p. S841.
2. Evidence, vol. 4, p. S841.
3. Evidence, vol. 4, p. S841.

Tax sub-program to not require separate evaluation. The Child Support sub-program was not evaluated in detail, however its position within the taxation system was considered.

3.8 The Committee noted that the four sub-programs encapsulate three quite distinct functions for a bureaucracy. The Income Tax and Sales Tax sub-programs are quite specifically revenue oriented. The Corporate Support sub-program targets the existence and maintenance of the bureaucracy of the ATO and the Child Support sub-program performs a socially targeted objective which utilises the structures of the taxation system for achieving a utilitarian outcome.

3.9 To the extent that the Government has the constitutional right to employ resources within the ATO for principally social rather than revenue collection objectives, the Committee considered the current program structure to be appropriate. The Committee found the patent social goal inherent in functions such as the Child Support Agency to provide a valuable link between the objectives of revenue collection and social utilitarianism.

3.10 In implementing the four sub-programs the ATO utilises the services of over 18 000 full-time and part-time staff through branch offices established in all capital cities and major urban and regional locations.⁴

3.11 Management of branch offices rests with Deputy Commissioners of Taxation, positions developed originally as the State based administrators of the Commonwealth's Land Tax law. Both the current role and title of the Deputy Commissioners is thus curiously anachronistic. Responsibility for the delivery of program objectives is shared between Deputy Commissioners and National Program Managers.⁵

3.12 Central management of the organisational structure of the ATO is provided by the Management Board (the Board). The Board sets the corporate policy direction for the ATO and is the peak internal advisory body to the Commissioner. Each branch office mirrors the Board with management committees.⁶

4. Evidence, vol. 5, p. 1515.

5. Evidence, vol. 4, p. S841.

6. Evidence, vol. 4, p. S841.

3.13 Advice to the Board is provided by both standing and ad hoc subcommittees. Apart from those subcommittees established to consider individual projects, the following subcommittees have been created for the purpose of providing specific advice to the Board:

- . the Human Resource Management Subcommittee;
- . the Program Co-ordination Subcommittee;
- . various Market Subcommittees;
- . the Committee for Professional Excellence; and
- . the Evaluation Committee.⁷

3.14 In addition, the Commissioner is provided with advice from parties external to the ATO through the Commissioner's Advisory Panel and the National and State based Tax Liaison Groups.

3.15 Membership of the Board currently consists of:

- . the Commissioner;
- . the three Second Commissioners;
- . three nominated National Program Managers;
- . two Deputy Commissioners; and
- . a representative of the Public Sector Union.⁸

3.16 While the Board has the capacity to set high level goals, objectives and strategies for the ATO and to monitor achievements, the day to day general administration of the taxation system, and thus the responsibility for the full operation of the ATO, is vested with the Commissioner.

7. Evidence, vol. 4, p. S841.

8. Evidence, vol. 4, p. S848.

3.17 The organisational relationship between the national office management (the Commissioner, Second Commissioners, Tax Counsel and National Program Managers) and branch office management (Deputy Commissioners) was described by the ATO in its submission to the Committee in the following terms:

The roles of the Commissioner, National Program Managers, Deputy Commissioners and Chief Tax Counsel are connected vertically and laterally to share within the top team the overall burden of policy setting and management and to enable consistency in operations. Roles are defined, but formal structures (subject to the carrying out of statutory powers) have been de-emphasised as senior executives embrace team approaches to management of the ATO and its business.⁹

3.18 Figure 3.1 sets out the organisational structure of the ATO as at 1 June 1993.

Efficiency of the Current Administrative and Organisational Structures

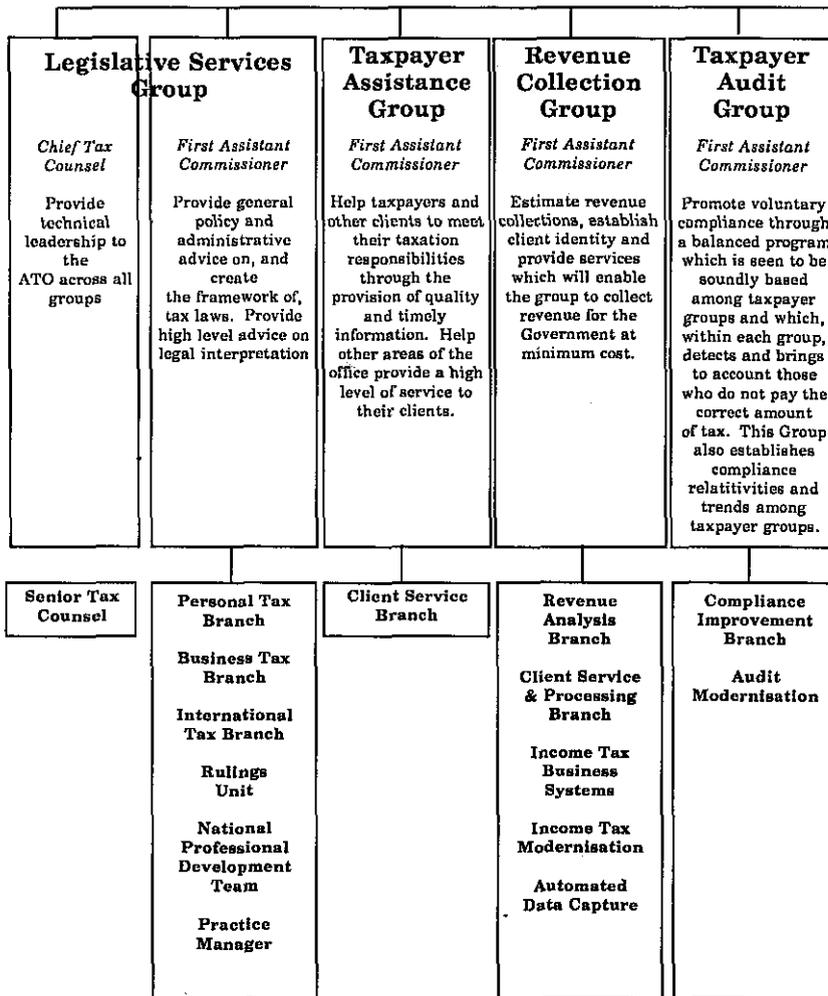
3.19 In its submission the ATO described its management structure as a 'matrix'. The objective of this structure was to 'break down organisational barriers and create ATO 'oneness'.¹⁰ The need to bring cohesion and disbursed contribution to the management of the ATO stemmed, in the Committee's view, from the generally fragmented nature of the ATO's administration of a national program. The historical emphasis on branch office control over strategy and administration was considered by the Committee to have contributed to unnecessary administrative complexity and uncertainty.

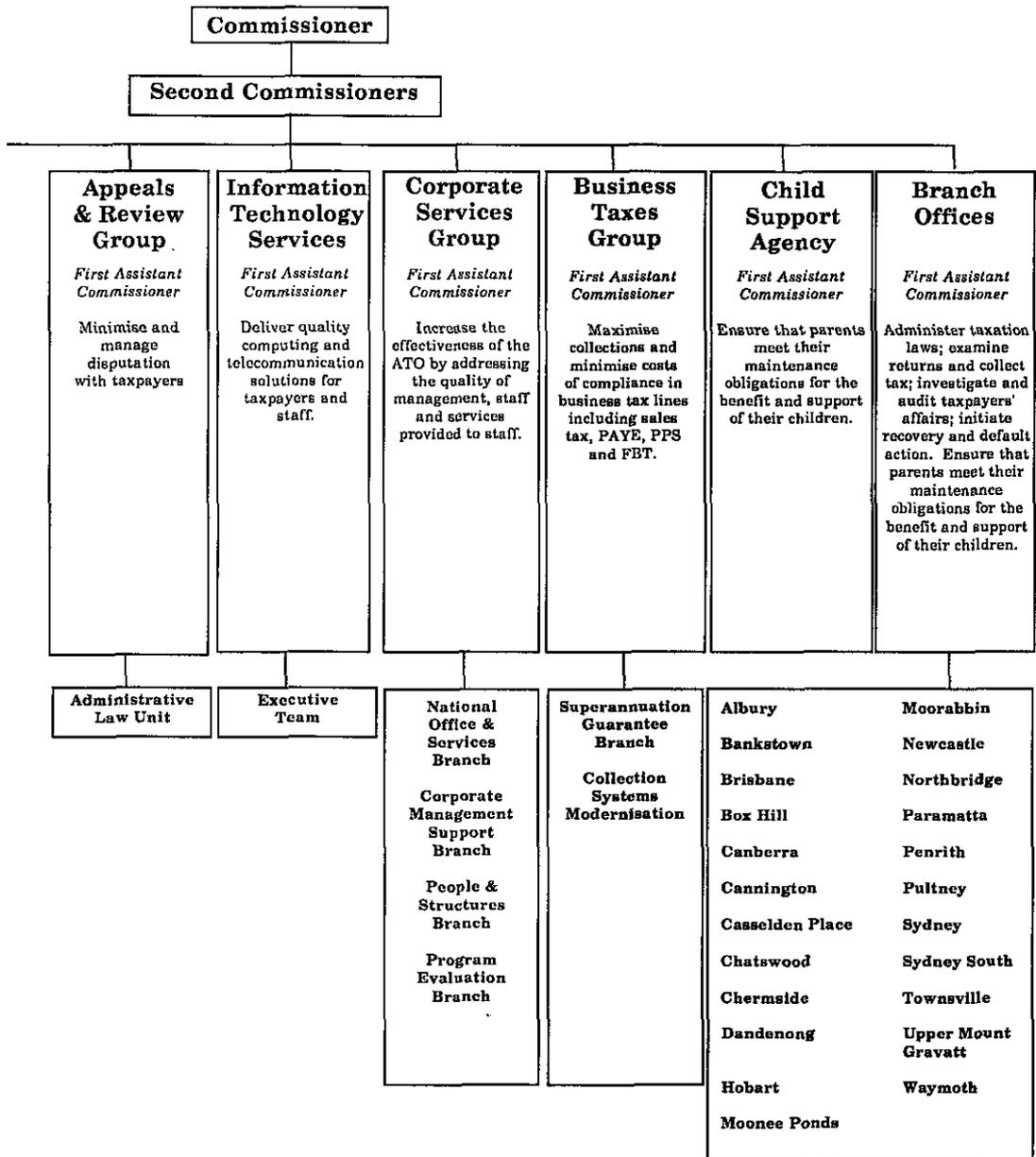
3.20 The Committee was cognisant that any assessment of the efficiency of particular administrative structures necessarily involves subjective judgements about what the current structure achieves and what might be achieved by any alternative.

9. Evidence, vol. 4, p. S844.

10. Evidence, vol. 4, p. S844.

**Figure 3.1 Australian Taxation Office Organisation Structure
As at 1 June 1993**





3.21 In considering alternatives, the Committee acknowledged that the current program of modernisation, including decentralisation and self assessment were integral to ATO planning. Nevertheless, the Committee was of the view that all changes in the ATO's structures which impacted upon taxpayers should seek to provide efficiencies for the Australian economy.

3.22 Given that the current administrative and organisational structures have not significantly altered since 1946, it would be reasonable to suggest that they have served the ATO well. However, in the Committee's view three factors have so significantly impacted upon the ATO's operations as to call into question the continued suitability of the current structures. They are:

- . the establishment of a national program structure in 1986-87;
- . the development of socially oriented functions for the ATO, in particular the Child Support Agency; and
- . the continued internationalisation of the Australian economy.

National Program and Group Structure

3.23 A national program structure has enabled the ATO to concentrate on the delivery of those objectives and targets which are inherent across the national economy. Consistency in policy development has been facilitated because the objectives can be couched in nationally relevant terms rather than having to be tailored to locally specific criteria. In addition, the development and refinement of organisational groups has established the roles and functions of the ATO and provided a nexus between each of these functions and the corporate objective.

3.24 The Committee considered the development of a national program structure to have been a sensible and relevant response to the nationalisation of the domestic economy. Within the national program structure, the Committee considered the development of the group, or functional, establishment. It noted the continuing development of service lines and in particular, the orientation of groups to service taxpayer requirements. In recognition of the objective of a more efficient interaction between the ATO and taxpayers, the Committee considered the development of functional groups aligned to taxpayer segments to be an appropriate advancement. At the time of preparing this Report, the Committee had not been able to review the outcome of a report to the Commissioner from a working party with input from the

world renowned Boston Consulting Group. The Committee concurred, however, with the objectives of the review as outlined in a submission from Commissioner Carmody.¹¹ In addition, the Committee noted that the recommendations of that review were currently the subject of discussions within the ATO.

3.25 The Committee has made recommendations in this Report for reform of a number of the current Groups within the ATO and considers these changes should be introduced regardless of the management structure ultimately adopted by the ATO.¹²

Social Objectives and the Changing Role of the Australian Taxation Office

3.26 In the last five years the ATO has been required by the Government to undertake revenue collection functions which can most appropriately be aligned to social policy objectives rather than general revenue gathering. That is, the Government has utilised the expertise of the ATO in revenue collection for the purposes of advancing social schemes. The most obvious example of this has been the function performed by the ATO under the Child Support Scheme.

3.27 While the Committee did not closely scrutinise the operations of the Child Support Agency, it considered four organisational features. Firstly, the Agency is established within the ATO as a separately identifiable Group. Thus, the uniqueness of the organisation is clearly recognised. This contrasts with the treatment of other areas of social policy which have been allocated to the ATO. In particular, the collection responsibilities for the Higher Education Contribution Scheme (HECS), Medicare, the Superannuation Guarantee, and the Training Guarantee Levy.

3.28 Secondly, the staff of the Child Support Agency have been largely recruited from within the ATO. While this has assisted in integrating the Agency within the ATO, it raises questions regarding the necessary skills levels for staff working on Child Support activities.

3.29 Thirdly, the Committee considered the resources available to the Child Support Agency in their broadest terms. Comments on this aspect are included in Chapter 8.

11. Evidence, vol. 18, p. S4136.

12. Legislative Services, Taxpayer Audit and Appeals and Review Group - see Chapter 11; Taxpayer Assistance Group - see Chapter 10; Revenue Collection Group - see Chapter 9.

3.30 Finally, the Committee considered the intellectual link of placing an operation responsible for enforcing parental responsibility for child maintenance within a taxation administration and the administrative response of the ATO to this 'offspring'. While the ATO stated that it considered the establishment of the Child Support Agency to have been beneficial to the ATO because it had softened its appearance, the Committee noted that the operation of the Agency within the ATO was not universally accepted.¹³

3.31 At an organisational level, the Committee considered the Child Support Agency demonstrated a clear and valuable link between the role of a taxation system and social utility. What was not clear to the Committee however, was whether the integration of a single purpose function within the ATO could be administratively managed using the same structures as those established over eighty years for general tax collection. The duties, roles, functions and skills requirements of the Child Support Agency were considered to be significantly different from that applicable to the primary areas of taxation administration.

3.32 While the Committee did not believe these differences meant the Agency should not be established within the ATO, it was concerned that the administrative structures and accountability channels within the organisation should appropriately reflect the imperatives of child support and not merely revenue collection.

3.33 The operation and effectiveness of the Child Support Scheme is currently the subject of an inquiry by the Joint Select Committee on Certain Family Law Issues and the Committee will await the report of this inquiry with interest.

Internationalisation of the Australian Economy

3.34 Technology, together with the advent of the international corporate entity and the further movement of Australia towards a full international market economy, has required the ATO to extensively re-fashion its horizons. International corporate transactions involve an unparalleled degree of complexity. International movements of currency can be instantaneous and audit trails are made inevitably weak. The legal status of taxpayers may be difficult to determine and the political implications of particular taxation policies may have ramifications for many countries and governments.

13. Evidence, vol. 1, p. S43.

3.35 Evidence presented to the Committee on the implications for taxation of the international nature of the Australian economy indicated the immense challenge which faces the ATO in the future.¹⁴ The Committee recognised that structural changes to the administration of the current system alone, may not be sufficient to produce an efficient outcome and that taxation laws may need to be varied or amended. However, such considerations fell outside the Committee's terms of reference and were not examined.

3.36 The Committee did however regard the future for the ATO as necessarily embracing a strategic focus, particularly in its administrative and auditing structures, which was inherently geared to the international marketplace.

Senior Management Structure - Proposals for Change

3.37 The Committee received a number of submissions referring to proposals to restructure the senior management structure of the ATO. Amongst these, the concept of a Board of Management for the ATO was proposed.¹⁵ Those in favour of the creation of such a body suggested that a Board would allow external points of view to be brought directly to bear upon the senior policy decision making processes. Others cautioned against a Board of external parties on the basis of vested interests and possible bias.¹⁶

3.38 In the Committee's opinion, the administration of the ATO and the taxation system generally would benefit significantly from the injection of opinions and strategies developed externally to the culture of the ATO. Moreover, the Committee recognised a need to expand the base of responsibility for the taxation system's administration. In both the development of administrative policy and in the implementation of specific taxation projects, the Committee considered there was significant advantage in drawing on the expertise existing outside the ATO's formal administrative structures. The Committee recognised that advisory committees could provide only limited input into general administration. At the same time, the Committee believed that the complexity of future taxation administration in an international economy would necessarily require the utilisation to the fullest extent possible of all commercial, strategic and organisational skills available both within Australia and from overseas.

Advisory
Committee

3.39 The Committee considered several options for the senior structure of the ATO's administration and concluded that, when considered in the broadest

14. Evidence, vol. 3, p. 548.
15. Evidence, vol. 3, p. S477; vol. 7, p. S1061.
16. Evidence, vol. 3, pp. 361, 435.

possible context, there was considerable merit in restructuring the ATO to create an Australian Taxation Commission.

3.40 The establishment of a formal Commission would, in the Committee's view, achieve five goals. Firstly, the administrative independence of the Commission from the administrative structure of the Treasury would be made clear. This would serve to highlight the separation between the roles of policy development and administration and would remove any suggestion that the ATO was controlled by or in some way beholden to the Treasury.

3.41 Secondly, the Commission's Charter could provide for the appointment of both full-time and part-time Commissioners. In this way the Government would be able to appoint senior executives with appropriate expertise to perform specific tasks within the taxation system. As these appointments could specify a duration, the Committee considered it would be more likely that the Government could attract and retain the most suitably qualified persons. In addition these roles would be clearly defined and the organisational structure of the Commission adjusted, as necessary, to manage the relative priorities within the system, as established from time to time.

3.42 Thirdly, while the general power of administration would continue to be vested in a Chief Commissioner, the collegiate style of administration pioneered by the ATO over the last decade could be utilised for the management of the Commission. Commissioners could be responsible for particular aspects of the tax system's operations with the possibility that consultative and advisory committees could also be established on an as required basis. For example, a Commissioner might be made responsible for tax law interpretation and the establishment of a Rulings committee. This committee could comprise officers of the Commission and external parties and would review all draft rulings prior to their release. The responsible Commissioner would then relay details of decisions of that committee and/or details of the Rulings to the rest of the Commission for formal approval.

3.43 Fourthly, with the Taxation Commission being responsible for programs of social importance, specialist administrators familiar with the problems of implementation and structures could be utilised as agency heads, whether on a full or part-time basis and for whatever period of time was deemed appropriate. The Chief Commissioner would thus not need to be the Child Support Registrar if the Government so determined.

3.44 A fifth benefit of a Commission would be the capacity to align position designations with those in the wider Australian Public Service. With a Chief Commissioner and full and part-time Commissioners comprising the executive body of the Commission, the Committee considered it meritorious to review the

designations applying to the staff of the Commission. The Committee considered it appropriate, for the convenience of the public, to align staff designations with those applicable to other Commonwealth bureaucracies and thereby to reflect the functional as well as geographic areas of responsibility.

3.45 The Committee recognised that certain Commonwealth Acts would need to be amended to achieve its preferred option. In particular, the Committee considers there should be an Australian Taxation Commission Act to establish the Commission and provide its charter of operation.

3.46 **The Committee recommends that:**

- . **the Australian Taxation Office be established by statute under its own Charter as the Australian Taxation Commission; and**
- . **the general power of administration of taxation Acts be vested in the Commission's Chief Executive Officer who shall be known as the Chief Commissioner of Taxation.**

3.47 In making this recommendation the Committee identifies the following key elements in a preferred model for the Australian Taxation Commission:

Composition

The Commission shall consist of:

- . a Chairperson, appointed by the Government, who may be a full-time or part-time Commissioner;
- . five full-time Commissioners, one of whom shall be Chief Commissioner; and
- . three part-time Commissioners.

Appointment

- . The Chief Commissioner shall be appointed for a fixed period of seven years;

- . the remaining four full time Commissioners shall be appointed for a maximum term of seven years;
- . the three part-time Commissioners shall be appointed for a maximum term of three years; and
- . all Commissioners including the Chief Commissioner may be reappointed.

Powers

- . The power of general administration of taxation legislation shall rest with the Chief Commissioner. The Chief Commissioner shall have the power to delegate the administrative powers to staff of the Commission.

3.48 All terms and conditions of appointment as apply to the current Commissioner and Second Commissioners, except for the duration of appointment which should be as outlined above, should continue to apply to the appointment of full-time Commissioners. In particular, the Commissioners should continue to be appointed by the Governor-General and dismissal would only be in those limited circumstances outlined in the *Taxation Administration Act 1953*.

3.49 It should be noted that, in order to implement the preferred model, the Committee believes that the position of Chairperson and Chief Commissioner should not be held concurrently by the same person. The Committee also envisages that the current Commissioner and Second Commissioners would be appointed as Chief Commissioner and full-time Commissioners, at least for the remainder of their current terms.

3.50 The Committee considers it appropriate that the Chief Commissioner of Taxation, with the consent of the relevant Minister, be able to determine the staffing and recruitment of the Commission within a global budget allocation. Providing employment flexibility to the Commission would reduce the concerns raised during the Inquiry about the potential loss of high level technical staff to the private sector. This matter is further discussed in Chapter 8.

3.51 For accountability reasons and in recognition of the significance of the Commission, the Committee considers it imperative that the Commission continue to report to Parliament in accordance with current practice. In particular, the Commission should be required to report separately all salaries and administrative expenses outlays within running costs and be subject, on an on-going and as required basis, to scrutiny by the Parliament.

3.52

Thus the Committee recommends that:

- . **the Australian Taxation Commission be established with a one line budget appropriation;**
- . **the Chief Commissioner of Taxation be able to recruit and employ staff on terms and conditions determined by the Chief Commissioner with the agreement of the Treasurer; and**
- . **the Australian Taxation Commission report on its resources to the Parliament in accordance with the current practice of the Australian Taxation Office and be fully available for on-going scrutiny by the Parliament.**

3.53 With a global budget the Commission would be able to determine its spending priorities. This would mean meeting all Commonwealth government budgetary requirements, including the payment of superannuation for employees, from within a given resource allocation. The Committee does not believe there is a need for the Commission to operate its own bank account nor to have investment powers. Within a global budget the Department of Finance should be capable of reflecting the outcome of such flexibility through adjustments to the Commission's budget. Moreover, the Committee anticipates that the majority of staff of the Commission will continue to be appointed, and have their terms and conditions determined, under the *Public Service Act 1922*.

3.54 Through the creation of a Commission, the Committee considered the on-going reforms and modernisation of the ATO could be further developed and enhanced. Establishing avenues for external involvement in the highest levels of administration of the taxation system, creating an independent organisation responsible for tax administration and providing full control over the resources necessary to perform taxation administration, were perceived by the Committee to represent the most significant merits of the proposed management structure.

International Comparison

3.55 In reaching its conclusion as to the desirability of a Commission, the Committee considered the current executive administrative arrangements in two international jurisdictions: the Internal Revenue Service (IRS) in the United States of America and the United Kingdom's Board of Inland Revenue.

United States of America Internal Revenue Service

3.56 The IRS is a bureau within the US Treasury Department. It is responsible for administering and enforcing the internal revenue laws and related statutes, except those relating to alcohol, tobacco, firearms and explosives. Its mission is to collect the proper amount of tax revenue at the least cost to the public, and in a manner that warrants the highest degree of public confidence in the IRS's integrity, efficiency and fairness.

3.57 The holder of the Office of the Commissioner is appointed by the Secretary of the Treasury and assisted by a Senior Deputy Commissioner, two Deputy Commissioners and 14 Assistant Commissioners.¹⁷

3.58 Organisationally the IRS is decentralised and operates from a national office based in Washington, DC, seven regional offices, 62 district offices and ten service centres. The national office is responsible for the development of policies and programs for the administration of the internal revenue laws. Each of the seven regional offices is headed by a Regional Commissioner who is responsible for the supervision and review of the performance of district offices and service centres.¹⁸

3.59 Each district office, administered by a District Director, is responsible for the provision of taxpayer services including:

- . examination;
- . Determination of tax liability;
- . collection;
- . criminal investigation; and
- . resource management.¹⁹

17. (US) Congressional Quarterly, *Federal Regulatory Directory*, 6th edn, Congressional Quarterly, Washington DC, 1990, p. 837.

18. (US) Office of the Federal Register, National Archives and Records Administration, *The United States Government Manual 1993/1994*, US Government Printing Office, Washington DC, July 1993, p. 505.

19. (US) Congressional Quarterly, loc. cit.

United Kingdom Board of Inland Revenue

3.60 The Commissioners of Inland Revenue (the Board), under the supervision of Ministers, are responsible for the administration of a number of taxes in the United Kingdom, including income tax, corporation tax and capital gains tax.²⁰ The Inland Revenue Department (the Department) is the third largest government department in the United Kingdom with in excess of 70 000 personnel operating out of 1 000 offices.²¹

3.61 The Board is empowered to appoint inspectors and collectors of taxes who act under its direction. Employees of the Board are civil servants and are formally under the control of the Treasury. The statutory Board consists of a Chairman, two Deputy Chairmen and two other Commissioners.²² Each of the Deputy Chairmen and Commissioners are responsible for the administration of discrete areas of the Department.

3.62 On 6 March 1992, the Chancellor of the Exchequer announced that a new Management Board would be formed as part of an ongoing program of reforms. It was intended that the new Board would comprise the existing Board members, other senior managers and a number of members from the private sector in a part-time capacity.

3.63 In addition, the Department was reorganised into a series of accountable management units; namely, the Valuation Office Agency, and 34 Executive Offices. Operational offices were grouped into two Operational Directorates, each with a Director of Operations reporting to the Chairman. Subject Divisions were created to specifically advise the Economic Ministers on technical and policy issues, review the performance of the Operational Directorates and suggest new ways in which services could be provided. Central finance and personnel functions were reduced in size.²³

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20. *British Tax Guide*, CCH Editions Limited, Bicester UK, October 1993.
21. (UK) Board of the Inland Revenue, *Report of the Commissioners of Her Majesty's Inland Revenue, for the Year Ending 31st March 1993, One Hundred and Thirty Fifth Report*, HMSO, London, September 1993, p. 9.
22. (UK) Board of Inland Revenue, *Report of the Commissioners of Her Majesty's Inland Revenue, for the Year Ending 31st March 1992, One Hundred and Thirty Fourth Report*, HMSO, London, November 1992, p. 10.
23. *ibid.*, p. 11.

3.64 The Committee noted that the Inland Revenue Department was continuing its reform process with particular focus on:

- . reorganisation of the office structure;
- . the simplification and streamlining of work procedures;
- . the use of information technology; and
- . the management of work and people.²⁴

3.65 The Committee acknowledges the distinct differences between the administrations and jurisdictions of the IRS, Inland Revenue and the ATO. To the extent that the respective administrations seek to reflect the priorities of their respective economies, the Committee considers comparative analysis useful. However, it recognises that significant differences in the structure of the various economies and tax arrangements, limit the capacity to transplant or impose one system upon another.

Revised Management Structure

3.66 The Committee considered the effect a change in the senior administrative structure would have upon the roles and responsibilities of senior management.

Role of Chief Commissioner

3.67 As previously mentioned, the Commissioner of Taxation currently has responsibility for the general administration of various taxation Acts. The Commissioner is also the Child Support Registrar. The *Taxation Administration Act 1953* establishes the position of Commissioner of Taxation and provides for the duration of the Commissioner's appointment, remuneration, resignation, the method for filling the office of Commissioner on a temporary basis, and how the Commissioner may be suspended or removed from Office. The Act also establishes the capacity of the Commissioner to delegate both powers and functions under a taxation or any other law.²⁵

24. (UK) Board of the Inland Revenue, *Report of the Commissioners of Her Majesty's Inland Revenue, for the Year Ending 31st March 1993, One Hundred and Thirty Fifth Report*, HMSO, London, September 1993, p. 12.

25. *Taxation Administration Act 1953*, ss. 5-6, 8-9.

3.68 The power of general administration is not defined in the *Taxation Administration Act 1953*. However, as the words imply, the power is general and not limited. Principally the power of administration requires the Commissioner to ensure that the will of Parliament as set out by law is properly administered to give effect to the terms of that law. Thus, where a taxation act imposes a tax it is the Commissioner's responsibility to determine the extent of the burden of taxation imposed by that law and the person or entity who should, according to the law, bear that burden.

3.69 In terms of principle, this power is similar to that given to Ministers of the Crown to administer the various laws of the Commonwealth. To the extent that the Commissioner exercises such powers in respect of taxation laws, the Commissioner is placed in a position which is more analogous to that of a Minister rather than a departmental Secretary, whose authority is delegated and not principal.

3.70 As well as being responsible for the general administration of taxation legislation, the Commissioner is responsible for the general working of the ATO. This stems from ss. 25(2) and 25(4) of the *Public Service Act 1922*. The latter subsection provides that the Commissioner has all the powers of, or exercisable by, a departmental Secretary under the *Public Service Act 1922* so far as the branch of the Public Service under the Commissioner's direct control is concerned. That branch is in effect a Taxation Branch of the Commonwealth Department of the Treasury. By virtue of the definition of 'Department' in the *Public Service Act 1922*, the ATO is treated as a separate Department in so far as the Commissioner's powers of administration are concerned.

3.71 It is possible for a Commissioner to identify certain matters over which he alone will exercise particular scrutiny in the operation of the administration of the ATO. For example, former Commissioner Boucher identified the following areas for his personal attention:

- . ATO business directions;
- . building and maintaining good external relations;
- . taxpayer help and promoting the service philosophy; and
- . Senior Executive transfers and promotions.²⁶

26. Evidence, vol. 4, p. S845.

3.72 The Committee noted the extensive responsibilities of the Commissioner of Taxation. In the Committee's opinion the proposal to establish a Commission would not prima facie alter the basic responsibilities of the holder of the current Commissioner's Office.

Accountability

3.73 In light of the proposed restructure, the Committee considered how accountability for the administration of the taxation system should be achieved and how control should be exercised between the Parliament, the Executive and the Commission. Included in the taxation legislation which provides the Commissioner with the general power of administration, is a requirement for the Commissioner to provide a report to the Minister on the operation of the Act.²⁷ The Minister is then required to have a copy of the report placed before the Parliament.

3.74 In this way, the Commissioner's administration powers derive directly from the Parliament, through an Act. The Commissioner is accountable for the performance of those powers back to the Parliament, via an Executive Government Minister. However, the relevant Minister cannot be considered to be accountable for the actions of the Commissioner as the Minister has no authority to instruct the Commissioner in the exercise of the relevant powers. Furthermore, the Parliament has no capacity to control the Commissioner other than, as a last resort, by acting to remove the statutory position of Commissioner and giving the general administration power to a Minister.

3.75 Under the *Taxation Administration Act 1953*, the Commissioner can only be removed from office on the grounds of proved misbehaviour or physical or mental incapacity.²⁸ The Committee doubted whether 'proved misbehaviour' would include administration of a taxation Act in a manner not considered appropriate by the Government or even the Parliament. For example, failure to devote sufficient resources to adequately capture the full extent of revenue potentially collectable under the Fringe Benefits Tax provisions, would most likely not amount to misbehaviour as that term is commonly understood.

3.76 In the Committee's opinion a 'gap' existed in the accountability chain currently applying to the Commissioner's general power of administration, and believed exercise of the general taxation administration powers should require more than just annual reporting as an accountability mechanism. The Committee considered that imposing an external review body over the Commission would serve

27. For example see *Income Tax Assessment Act 1936*, s. 14.

28. *Taxation Administration Act 1953*, s. 6C.

only to further remove accountability from the Parliament.²⁹ Consequently the Committee considered that the Parliament should be able to hold the relevant Minister responsible for the exercise of the general taxation administration powers.

3.77 To be able to do this however, the Committee considered accountability principles required that the Minister have the capacity to instruct the proposed Chief Commissioner in the exercise of the administration powers. This was considered appropriate as democratic principles required that elected representatives should be accountable for those actions which affected citizens. The current situation was considered unsatisfactory by the Committee because no certainty of responsibility existed between the relevant parties.³⁰

3.78 While the Committee did not consider that the issuing of 'directions' would be common, it nevertheless recognised it as a potential course for a Minister. To ensure no improper influence over the proposed Chief Commissioner in the exercise of the general administration powers and to provide against improper use of the power of direction, the Committee considered it appropriate that the Minister should table in both Houses of the Parliament within five sitting days of issuing any direction, a copy of that direction. In this way, the Minister possessed an avenue for affecting the exercise of the general administration powers without removing those powers from the proposed Chief Commissioner. In addition the Minister would be responsible to the Parliament for the exercise of the powers.

3.79 The Committee is concerned at the possible breach of independence which could be considered to flow from allowing directions to be issued concerning the exercise of administration powers. In the Committee's opinion, the proposed Chief Commissioner's independence would be maintained by the nature of a statutory appointment, the strict conditions applying to removal from office and the requirement that any direction issued by the Minister would be of no effect if it were not tabled in both Houses of Parliament in accordance with the given procedure. The Committee further considers that the power of direction should not apply in respect of the application of taxation laws to particular taxpayers.

29. Evidence, vol. 14, p. S2779.

30. Evidence, vol. 7, p. S1152.

The Committee therefore recommends that:

- . in order to reinforce the independence of the Chief Commissioner, so much of the taxation laws of Australia be amended as would allow the Minister responsible for taxation matters to issue directions to the Chief Commissioner of Taxation concerning the manner in which the Chief Commissioner exercises the general powers of administration conferred on the Chief Commissioner by the various taxation laws;
- . the relevant Minister responsible for taxation matters be required to table before both Houses of the Parliament within five sitting days of having issued a direction to the Chief Commissioner of Taxation in respect of the exercise of the general powers of administration, a copy of the relevant direction;
- . until the relevant Minister has satisfied the requirement to table the issued direction, the said direction shall have no effect and the Chief Commissioner of Taxation shall not be required to comply with the said direction; and
- . the power to issue directions not apply in respect of the application of taxation laws to individual taxpayers.

3.81 As part of the framework for the accountability of the proposed Chief Commissioner to the Parliament the Committee considered the issue of privacy. The secrecy of taxpayers' affairs is a matter of the greatest importance to the ATO, with secrecy enshrined legislatively in s. 16 of the *Income Tax Assessment Act 1936* and s. 3C of the *Taxation Administration Act 1953*. Although parliamentary committees are not bound by such provisions, the Committee considers the secrecy of taxpayers' affairs to be a principle worth preserving. In the Committee's view, avenues of redress for taxpayers who allege abuse of power already exist and in the absence of evidence of any systemic abuse of power or corruption, there is no need for the Parliament to access taxpayer records or review individual cases with the ATO. Moreover, the Committee acknowledges that while there is a need for the Parliament to maintain a close scrutiny over the administration of the taxation system, many investigations and inquiries involving consideration of the operations of the ATO have been conducted over the past ten years.

3.82 Although the Committee will continue to take a close interest in the activities of the ATO, it recognises that there are a number of formal channels of investigation and review already scrutinising the ATO. In particular, supervision and investigation is provided by the:

- . Commonwealth Privacy Commission;
- . Commonwealth Ombudsman;
- . Australian National Audit Office; and
- . Bi-annual Senate Estimates Committees.

3.83 The Committee considers that when taken together, these avenues of scrutiny provide a comprehensive and extensive network of accountability.

Reporting Requirements

3.84 While the current Commissioner exercises all the powers of a departmental Secretary so far as they relate to the ATO, he is not required by the *Public Service Act 1922* to prepare and furnish an annual report to the Minister on the operation of the office.³¹ Section 14 of the *Income Tax Assessment Act 1936* only requires the Commissioner to prepare and furnish a report 'on the working of this Act, including any breaches or evasions of this Act of which the Commissioner has notice.'

3.85 In the Committee's view it is a curious oversight that one of the Commonwealth's largest 'departmental' employers is not required to report annually in the same manner as other departments.³² The Committee believes that the proposed Chief Commissioner should be required to report to the Parliament and should be required to comply with the guidelines for the preparation of annual reports in the same manner as all other departments. Clearly a significant amount of material currently reported in the Commissioner's Annual Report on the operation of the various Acts under his administration, would continue to be incorporated in any report pursuant to the *Public Service Act 1922*.

31. *Public Service Act 1922*, s. 25(9).

32. *Budget Statements 1993-94, Budget Paper No. 1*, AGPS, Canberra, 1993, p. 3.305.

3.86 The Committee recommends that:

the *Public Service Act 1922* be amended to require the Chief Commissioner of Taxation to report annually to the Minister on the operations of the Australian Taxation Commission; and

the Chief Commissioner be required to comply with so much of the guidelines for annual departmental reports as would not involve breaches of Section 16 of the *Income Tax Assessment Act 1936*.

3.87 By requiring the proposed Chief Commissioner to furnish the Minister with an annual report on the operations of the Commission, the Committee seeks to reinforce the obvious administrative links between the Commission, the proposed Chief Commissioner and the Government. The Committee could see no value in constructing a theoretical framework of administrative isolation and independence around the Commission, in so far as its task of administering the taxation laws is concerned, when the resources necessary to perform that task are directly the responsibility and choice of the executive government. The proposed Chief Commissioner, as a Public Service head, must be cognisant of the political imperatives of the government of the day. This is particularly so in terms of an organisation responsible for the collection of the vast majority of the Commonwealth's revenue and one which spends approximately \$1 billion a year in the collection of that revenue.

Second Commissioners

3.88 The current offices of Second Commissioners of Taxation are established by s. 4 of the *Taxation Administration Act 1953* which gives to Second Commissioners similar powers to that of the Commissioner of Taxation.³³ The history of the ATO demonstrates that the positions of Second Commissioner were established primarily to relieve the Commissioner of some of the burden of administration in an ever expanding tax collection system.³⁴ Subject to the power of general administration and the responsibility for reporting annually to the Parliament, the current three Second Commissioners exercise the same principal powers and functions as the Commissioner under taxation law.³⁵

33. See for example ss. 5A, 6, 6A, 6B, 6C.

34. The third Second Commissioner was appointed in 1985.

35. *Taxation Administration Act 1953*, s. 6D.

3.89 The roles of Second Commissioners in the administration of the ATO are, like the Commissioner's, not specifically defined. This lack of definition allows the Second Commissioners to be allocated responsibilities for which they are most skilled. Over time these responsibilities have altered both with changes to the relative priorities of the ATO and with changes in personnel and thus interests and skills. The Committee noted that both the specific duties of the current Second Commissioners and the relative distribution of responsibilities were amended following the appointment of the new Commissioner in January 1993.³⁶

3.90 The Committee considered the functions performed currently by the Second Commissioners would be most efficiently performed by Commissioners within the proposed Taxation Commission. With a larger number of executives acting in a collegiate manner, the Committee considered the administrative apex of the Commission would exhibit both flexibility and breadth of opinion.

3.91 The Committee recognised the flexibility that was occasioned by having no definitive charter for current Second Commissioners, and considered such an arrangement to be suitable for the Commission. The possibility of Commissioners exercising particular responsibility for groups or programs was considered by the Committee to be an option for the Government in the context of the Commission's general administration.

National Program Managers

3.92 The specific role of National Program Managers was described in the submission to the Inquiry from the ATO in the following terms:

- . to assist the Board and its subcommittees in the development of broad policy directions and objectives;
- . within those directions, develop the strategies, framework and setting for the operation of their Group, including national approaches (e.g. 'best practices' and structures) where appropriate;
- . determine and agree with Deputy Commissioners branch resources and expected outcomes within the parameters determined by the Board - these are reflected in the Integrated Resource Plan which in addition to Group specific outcomes, includes HRM

36. Evidence, vol. 4, p. S845; vol. 18, p. S4137.

directions and outcomes for the groups and branches as a whole; and

monitor the achievement of agreed resourcing and outcomes.³⁷

3.93 With a national taxation system and a significantly intertwined international and domestic economy, the imperative of a national perspective in target and priority setting was considered by the Committee to be critical. In this context National Program Managers are an important part of the ATO. As the title suggests, National Program Managers are primarily concerned with the application and performance of strategies for their respective Groups across Australia. Their focus must consequently concern consistent application of strategies regardless of any domestic circumstances which may pertain in a given State, region or office.

3.94 National Program Managers are administrative positions within the ATO. They are consequently positions created to achieve a management or operational objective. These positions were established within the national office in line with the formalisation of the ATO Group structure.

Deputy Commissioners

3.95 When the first Commonwealth Land Tax Act was passed in 1910, six Deputy Commissioners were appointed for the purpose of administering the new Act in each of the States. Today Deputy Commissioners are appointed pursuant to s. 7 of the *Taxation Administration Act 1953*. That provision allows for the appointment of as many Deputy Commissioners as are considered to be required - presumably to administer the taxation laws.

3.96 In its submission the ATO described the role of the Deputy Commissioners as the delivery, at an operational level, of the program strategies developed by the National Program Managers.³⁸ This function would appear to

37. Evidence, vol. 4, p. S846.

38. Evidence, vol. 4, p. S846.

place the Deputy Commissioners in a line responsibility below the National Program Managers. However, the ATO submission went on to state:

In particular, Deputy Commissioners are responsible for:

- . achieving agreed outcomes within resourcing allocations across all programs within their office and region;
- . taking responsibility for program operations during the year within nationally established objectives and approaches;
- . assisting National Program Managers ... in policy development;
- . operating within agreed corporate guidelines reflected in the Integrated Resource Plan, and any subsequent decisions of the Management Board;
- . implementing agreed measurements to monitor achievements, and supply necessary information to National Program Managers.

3.97 The submission continued:

In circumstances where there are problems in achieving agreed performance, Deputy Commissioners can move work, staff and budgets within and between programs where this is needed to achieve total branch objectives.³⁹

3.98 The apparent contradiction of a system which permits local decisions to dominate national priorities and elevates local objectives above the national, was considered by the Committee to be inappropriate. Moreover, the veto power of Deputy Commissioners in their own office was viewed by the Committee as a significant barrier to the achievement of consistency and co-operation in the application of a set of national operational standards. While local branch performance may be a useful indicator for internal evaluation, it was the overall performance and achievements of the entire ATO which will be ultimately judged by the Australian public as important.

39. Evidence, vol. 4, p. S847.

3.99 The Committee noted advice given to the ATO in 1990 to adopt an accountability regime based more on functional rather than geographic factors.⁴⁰ The status of Deputy Commissioners appeared to the Committee to be geographically and not functionally based. Moreover, the Committee considered the current role and description of Deputy Commissioners in the context of a Taxation Commission, to be misleading and inappropriate. Because of the Committee's view that there needs to be standardisation of the titles of Taxation Commission staff the Committee regards it as more suitable to describe the roles currently performed by Deputy Commissioners in terms of their functional and geographic areas of responsibility - be that State, regional or at the branch level - and that they would be better described as, for example, 'Branch' or 'Regional Directors'.

3.100 The Committee recommends that:

- . the functions of the current Deputy Commissioners of Taxation be couched in terms of branch or regional establishment management; and
- . the title of the current Deputy Commissioners of Taxation be amended to more accurately reflect their revised role.

External Advice

3.101 The ATO currently derives formal advice from parties external to the Office through two advisory committees:

- . the Commissioner's Advisory Panel (CAP); and
- . the Taxation Liaison Group (TLG).

Both committees are informal in that they have no statutory status within the administrative structures of the taxation system, have no permanent secretariat and members provide their services on a voluntary basis.

3.102 The committees grew out of moves in the early 1980s to open up the administration of the taxation system and to construct a mechanism for input and feedback from taxpayers, their representatives, and the community generally. The TLG developed from informal discussions between the Commissioner and tax

40. Evidence, vol. 2, p. S133.

professionals from the Australian Society of Accountants, the Institute of Chartered Accountants in Australia and the Law Council of Australia.⁴¹ The CAP was established in 1989 in an attempt to broaden the scope of community input into the advising role.

Tax Liaison Group

3.103 The first formal meeting of the national TLG was held in March 1985.⁴² Since then, TLGs have been established in most branch offices of the ATO for the purpose of discussing matters of a local or regional significance. The national TLG still operates.

3.104 At the national level, representatives from the following organisations were foundation members of the TLG:

- . the Taxation Institute of Australia;
- . the Institute of Chartered Accountants in Australia;
- . the Law Council of Australia; and
- . the Australian Society of Certified Practising Accountants.

3.105 Membership of the national TLG has been expanded over the years with representatives from the following bodies:

- . the Commonwealth Department of the Treasury (December 1986)
- . the Australian Taxpayers' Association (May 1987)
- . the National Institute of Accountants (July 1989)

3.106 Each organisation was selected because of its status as a representative of professional practitioners in the taxation system.⁴³ Each organisation is responsible for selecting its own representative for meeting purposes.

41. Evidence, vol. 4, p. S857.

42. Evidence, vol. 4, p. S857.

43. Evidence, vol. 1, p. 54.

Generally this representative is a senior official of the body or a senior spokesperson for the organisation's tax committee. Apart from issuing invitations to the respective bodies, the Commissioner has no input into the selection of representatives.⁴⁴ Representatives at branch or regional levels similarly derive from the above mentioned bodies as well as State Law Societies, State Taxpayers' Associations or the Taxation Institute of Australia.

3.107 As is evident from their constituent membership, TLGs are designed to act as professional forums for the discussion of issues of concern to professionals. In 1989 the national TLG agreed that discussions about taxation and legal policy were outside the role of the Commissioner and therefore the TLG. This recognition was however tempered to the extent that problems of administration which required legislative rectification could be considered.⁴⁵

3.108 The national TLG meets only four times per year in Canberra and is essentially reactive though issues for discussion are proposed by the TLG members. Throughout its history, the national TLG has had occasion to form subgroups for the purposes of conducting or evaluating research and discussion. Issues such as capital gains tax, Rulings and self assessment have been considered. A Charter for the national TLG was adopted in 1989. A copy of the Charter is at Appendix 7.

3.109 State TLGs generally meet quarterly depending on the extent of issues proposed for discussion. At the State level, the issues of concern for the TLGs tend to have a more local focus and in particular concentrate on the administration of policy by a particular branch office. At this level the TLGs act in concert with more specific forums organised by the regional or State offices. These additional forums tend to concentrate their activity on technical issues while the TLGs approach matters at a more general or principle level.

Commissioner's Advisory Panel

3.110 The first CAP met in Canberra on 9 May 1989. Apart from officers of the ATO, representatives of the following organisations were present:

- . the Council of Small Business Organisations of Australia;
- . the Business Council of Australia;

44. Evidence, vol. 1, pp. 54-7.

45. Evidence, vol. 4, p. S858.

- . the Australian Bankers' Association;
- . the Australian Tax Teachers' Association;
- . the Institute of Chartered Accountants in Australia;
- . the Law Council of Australia;
- . the Australian Council of Social Services; and
- . the Metal Trades Industry Association.

3.111 In July 1990, the Federation of Ethnic Communities Councils of Australia Incorporated joined the panel upon the resignation of the representative of the Australian Tax Teachers' Association.

3.112 The initial reasons for establishing the CAP are best summarised in the words of the Commissioner at the inaugural meeting:

With continuing community focus on the tax system and its delivery mechanisms, the ATO decided there was a need to seek input from wider interest groups in the community with significant interests in tax administration.⁴⁶

3.113 It was made patently clear to its members that the CAP was intended to replace neither the TLG structures nor other consultative mechanisms. The CAP was restricted from the outset to discussions of administration with the Commissioner making it plainly understood that questions of taxation policy and changes to the law would not be canvassed.⁴⁷ To the extent that law changes were purely of an administrative character, the Commissioner made it known that he could only act as a broker to the Government of the day.

3.114 To assist the CAP in its focus, the inaugural Panel adopted a Charter detailing how the committee would work. A copy of the Charter is at Appendix 8.

46. Evidence, vol. 10, p. S1605.

47. Evidence, vol. 10, p. S1605.

3.115 Evidence to the Committee on the operations of the advisory committees suggested there was general agreement about the merits of the consultation process that the ATO had undertaken. Tax auditors, however, expressed concern in regard to three particular features of the process:

- . the potential for committee members to exercise inappropriate influence in the administration of the ATO;
- . the selection process for membership of the committees; and
- . the duality of the roles of the two committees.

These matters are discussed below.

Relationship between Advisory Committee and Australian Taxation Office Staff

3.116 The Committee received evidence⁴⁸ alleging circumstances in which members of the advisory committees had, in their capacity as taxpayer representatives, sought to influence the administration of their client's audits through contact with an auditor's superiors. The auditors in question considered such actions were inappropriate given their responsibilities for carriage of particular cases.

3.117 The Committee found no evidence to suggest that advisory committee members, in making client representations, had acted other than on behalf of a client in such a manner as was generally open to any taxation professional or for that matter to any taxpayer. Moreover, there was no evidence that the standing of members of advisory committees was ever used as a lever for special treatment of clients. The representations described were evidently made for and on behalf of professional clients. It was submitted to the Committee by a former advisory committee member that members enjoyed no special access to senior levels of the ATO.⁴⁹

3.118 The Committee concluded that there was no evidence to suggest any impropriety on the part of any advisory committee member in their professional dealings with the ATO on behalf of their clients. However, the Committee acknowledged that there was always potential for advisory committee members who were active taxation practitioners to be perceived to possess a standing as a result

48. Evidence, vol. 3, pp. 715, 791, 802.

49. Evidence, vol. 2, p. S122.

of their committee membership. The Committee recognised the potential for the use of this standing as leverage in negotiations with case auditors. To protect auditors from improper motives, the ATO should establish a formal mechanism for the lodgement of complaints against auditors. Such a mechanism should at the very least require that complaints be lodged in writing. The Committee believes any complaint procedure must be comprehensive, effective, transparent and encourage only genuine complaints.

3.119 **The Committee recommends that:**

the Australian Taxation Office require all complaints against individual case auditors be put in writing.

Conflict of Interest

3.120 In evidence, concerns were raised with the Committee by officers of the ATO and others at an apparent conflict of interest that practising members of the accounting and legal professions may have when sitting on advisory committees.⁵⁰ This concern was expressed in terms of the interest that these professionals had in having certain issues decided in a particular manner - that is, in a way advantageous to their clients and not necessarily in the interests of good management the taxation system.⁵¹ The Committee was not given specific examples where this apparent conflict had arisen. Rather, the concern was merely expressed in terms of principle.

3.121 The Committee noted that advisory bodies have no formal standing within the ATO or taxation system. The Committee affirms the principle that the influence of any advisory committee members should only be dependant upon, and limited to, the strengths of the arguments they present.

3.122 When appearing before the Committee both the Commissioner and members of the advisory committees, fully acknowledged the interests that members represented when sitting on the advisory committees.⁵² However, it was made clear to the Committee that invitations to participate on committees were issued on the basis of an organisation not an individual. Invitations to professional groups had the inevitable consequence of leading to the presentation of particular points of view. It was so those views may be represented, that the groups were selected.⁵³ Indeed,

50. Evidence, vol. 2, p. 435; vol. 3, pp. 721, 792-3.

51. Evidence, vol. 3, p. S542; vol. 2, p. 416; vol. 3, p. 721.

52. Evidence, vol. 2, p. S121; vol. 1, p. 54.

53. Evidence, vol. 1, p. 55.

the fundamental role of the advisory bodies was to serve as a conduit through which input from a variety of professionals, tax practitioners and industry-based groups might be channelled to the Commissioner.⁵⁴

3.123 Whilst the Commissioner issues invitations to relevant organisations, the right to select an organisation's representative was, and remains, the prerogative of the organisation. The Committee considered this process to be fair, reasonable and appropriate.

3.124 As to the suggestion that representatives on committees should be rotated,⁵⁵ the Committee considered that no substantial benefit would flow from any prescription as to the length of time that individuals should be permitted to represent organisations. Indeed, the balancing of the merits of rotation with consistency was viewed by the Committee to be an issue best left within the province of the individual organisations whose positions were being represented.

3.125 The Committee considers that the method of composition of any advisory committee is appropriately one for the person or body seeking the advice. To the extent that the advice of professional bodies and organisations is sought, the Committee concludes that the current arrangements are satisfactory, provided the names of organisations consulted are publicly disclosed.

Duality of Operation

3.126 In considering the operation of the advisory committees within the current system, the Committee was struck by the duality of the functions performed by the national TLG and CAP. In evidence, it was proposed that the value of the advisory bodies was questionable.⁵⁶ While their roles and powers are limited by their position as non-statutory bodies, it would appear they have been generally successful as a mechanism for facilitating discussion. The Committee concluded, from the evidence of representatives who sit on the committees, that there was a dissatisfaction in the manner in which information was being handled by the committees and that this reflected upon the standing of the committees.⁵⁷ The Committee noted that a review of the procedures of the national TLG was being conducted for the purposes of improving efficiency.

54. Evidence, vol. 2, p. S121.

55. Evidence, vol. 3, p. S542; vol. 5, p. S673.

56. Evidence, vol. 2, p. 402.

57. Evidence, vol. 3, p. 649.

3.127 The Committee was concerned at the suggestion that to a certain extent the advisory committees were being used by the ATO to disseminate information to the professions and present decisions of the ATO as having been produced by consultation. Evidence was presented that in fact the advice of the professions was often disregarded or decisions announced which were quite contrary to the advice tendered.⁵⁸

3.128 While the Committee could not draw absolute conclusions as to the manner in which individual committees operated, it was able to ascertain a sense from witnesses that these committees had reached a point in their existence where something more decisive and fundamental was required. The Committee considered advisory committees could play a positive role in a revised ATO administrative framework. Specific committees established to interact with Commissioners of the proposed Australian Taxation Commission on identifiable projects, would in the Committee's view, provide valuable expertise and opinion.

3.129 The Committee considers that the current advisory system should be re-examined and more directly targeted to subjects and issues of significance to the general administration of the taxation system as determined by the Commission from time to time.

3.130 The Committee acknowledges the perception that it is possible for members of advisory committees, because of their professional duties, to be seen to have a conflict of interest in dealing with issues that may be relevant to their clients. The Committee considered the need for the establishment of a register of interests of members of advisory committees, but rejects this notion because the members of such committees would be likely to have large numbers of clients, and the difficulties of maintaining an up-to-date register would render this proposal impractical.

3.131 **The Committee recommends that:**

- . **the role of advisory committees be formalised and strengthened within an Australian Taxation Commission;**
- . **advisory committees be structured so as to play a positive role in the context of a revised administrative framework;**

58. Evidence, vol. 2, p. 400; vol. 3, p. 649.

- . **specific advisory committees be established as necessary, to interact with Commissioners of the Australian Taxation Commission on identifiable projects; and**
- . **the names of members of advisory bodies be published together with the names of the organisations they represent in the Annual Report of the Australian Taxation Commission.**

Chapter 4

SELF ASSESSMENT

- . History of Self Assessment
- . Efficiency and Effectiveness
- . Costs of Compliance
- . Proposals to Extend Self Assessment

4.1 One of the most significant developments in Australia's taxation system has been the move to self assessment. Under this system taxpayers are responsible for calculating their own tax liability and are encouraged to comply with the law by a number of means including targeted audits. This chapter provides an overview of the history of self assessment and examines its operation.

History of Self Assessment

4.2 Between 1983 and 1985 the Australian Taxation Office (ATO) examined income tax collection within Australia and conducted a limited examination of overseas experience. In particular, the method of taxation assessment was reviewed. Under the system of income tax assessment most commonly understood, a taxpayer would lodge a return containing information from which the ATO assessors would prepare a statement (an assessment) of the taxpayer's taxable income and tax payable. A 'notice of assessment' would then be issued and the amount payable would become a debt due in accordance with the statutory period for paying taxation debts.

4.3 A taxpayer had the right to object to the assessor's calculations of the debt due and the ATO was then required to review the taxpayer's case. By the early part of the 1980s this review procedure was placing considerable strain on the ATO's resources.¹ In 1983-84 the number of objections against assessment numbered in excess of 236 000.² Despite an intensive internal campaign to improve primary assessments, the possibility existed that if the annual percentage growth of returns disputed continued at the then existing rate, the ATO would ultimately have utilised more staff in reviewing assessments than in processing them.³

1. See Chapter 2.

2. Commissioner of Taxation, *Sixty-Third Annual Report*, AGPS, 1984, p. 8.

3. *ibid.*

4.4 Moreover, with approximately 10 million income tax returns to assess annually and with quotas applying to assessors, it had been calculated that, on average, an individual taxpayer's return would have received an optimum of one minute of scrutiny by the ATO assessors.⁴ Using the historical number of staff available for performing the assessment function, the same type of calculation suggested business returns would have been considered, on average, for four minutes.⁵ The number of returns each assessor was required to process in a day was determined in a manner as to effect maximum workflow. Wage and salary assessors were required to process as many as 400 returns in a day.

4.5 During 1983-84 an internal ATO committee began a fundamental review of the assessment process. The possibility of taxpayer self assessment was first mooted in the context of an attempt to determine the best basic approach for the future of the taxation system, having regard to 'the needs of revenue enforcement, taxpayer convenience and staff job satisfaction.'⁶

4.6 In 1985 an Assessing Review Group was established within the ATO and was required to consider whether the then system of assessment should be retained or replaced by some type of self assessment system. In determining this question, the Group was required to have regard to 'the need for the greatest practicable level of efficiency and effectiveness of the operations of the ATO.'⁷

4.7 The ATO considered the influencing factors on any proposal for change were:

- . immediate revenue effects;
- . the underlying impact on taxpayer compliance;
- . the effect on the level of disputation;
- . the level of taxpayer convenience; and
- . staff satisfaction.⁸

4. Evidence, vol. 4, p. S970.

5. Evidence, vol. 4, p. S970.

6. Commissioner of Taxation, op. cit., p. 9.

7. Evidence, vol. 4, p. S971.

8. Evidence, vol. 4, p. S971.

4.8 The Committee noted that the cost of a change to taxpayers was not included in the list.

4.9 In 1986-87 the first steps were taken towards a system of taxpayer self assessment. First stage self assessment was introduced through amendments to the *Income Tax Assessment Act 1936* which relieved the ATO of the obligation to examine returns in the process of assessment. Other changes introduced included:

- . an interest charge on unpaid tax to compensate for the cost of lost revenue between the period of assessment and the issue of an amended assessment;
- . the capacity of the Commissioner to amend for not only errors of calculation or mistakes of fact but also mistakes of law; and
- . a mechanism for taxpayers to seek information from the Commissioner in respect of an issue affecting the taxpayer's liability at the time a return was lodged.⁹

4.10 As a result of these changes, taxpayer returns containing details of income and expenses, and thus a calculation of the amount of taxable income were no longer subjected to technical scrutiny by the ATO. Resources freed from the process of assessment were reallocated to post assessment checking and taxpayer advising services. Technically the ATO continued to issue the assessment and thus create the necessary taxation debt. In practice however, the assessment was being made by the taxpayer in the sense that, at least in the first instance, the taxpayer's information contained in the return would not be checked for technical accuracy by the ATO.

4.11 In the ATO's view, first stage self assessment did not alter the obligations of taxpayers and the impact on taxpayers should have been negligible. Only the chance of being audited had changed.¹⁰ In the Committee's view this narrow perception of the impact of self assessment on taxpayers failed to grasp the importance of the shift in responsibility for assessing as a fundamental step in the administrative process. The removal of the 'check' step of ATO assessment, whether adequately performed or otherwise, placed added responsibility on taxpayers. Furthermore, the importance of the advising function in a self assessment system was grossly underestimated by the ATO. This was most dramatically evidenced by

9. Evidence, vol. 4, p. S972.

10. Evidence, vol. 4, p. S973.

the resources allocated to advising from the freed assessing function after the second stage of self assessment was introduced.¹¹

4.12 As a result of measures introduced in the 1989 Federal Budget, the returns of companies and superannuation funds for the 1989-90 financial year and all latter income years were subjected to a system of full self assessment. The difference between the first stage self assessment and full self assessment was described in 1991 by the then Treasurer:

The essential difference ... is that, under the latter system, the taxpayer goes one step further than working out taxable income by also calculating the tax payable on that income and sending that amount to the Tax Office with a return that contains only limited information. The Tax Office does not issue an assessment on the basis of the return lodged.¹²

Efficiency and Effectiveness

4.13 In a Government information paper issued in August 1991, it was claimed that self assessment was a more efficient method of collecting tax because it enabled the ATO 'to shift its primary focus from processing returns and issuing assessments, to helping taxpayers to meet their obligations, and taking enforcement action against those who [do not]'.¹³

4.14 Such claims raise two important questions. Firstly, is self assessment a more efficient revenue collection system and, if so, more efficient than what alternative? Secondly, is self assessment a more efficient system for taxpayers and thus the Australian economy as a whole?

4.15 The Committee considered the efficiency of a system of self assessment could only be compared to the position which existed prior to 1986-87 for the assessment of taxpayer returns, that is, assessment by the ATO.

11. Evidence, vol. 3, p. S580.

12. Honourable John Kerin, MP, Treasurer, *Improvements to Self Assessment - Priority Tasks*, An information paper, 20 August 1991, Commonwealth of Australia, 1991, p. 1.

13. *ibid.*

4.16 The efficiency of assessment by ATO assessors, particularly assessment of individual returns, was limited by the amount of time available for assessment and despite the skill of the assessor, it was inevitable that errors would occur in assessments. To perform the same assessment function today, would require a sizeable investment by the Government in additional resources for the ATO. It has been estimated that an additional 13 400 staff would be required for just four months simply to perform the assessment function for individual taxpayers. On the basis of calculations made by the former Commissioner of Taxation such a task would equate to an annual cost of somewhere in the vicinity of \$130 million.¹⁴ If the reported return from a dollar invested in audit resources is assumed correct, the potential return to the revenue of such an investment would need to be of the order \$1.3 billion to be cost effective in comparison to an investment in audit staff.¹⁵

4.17 In an evaluation of the first stage of self assessment in December 1989, the ATO concluded that the introduction of self assessment as an alternative to the former system of assessment was a sound approach to the income tax environment of the 1980s.¹⁶ The evaluation further concluded:

- . overall revenue results for the ATO indicated that the introduction of self assessment had a positive effect on income tax revenue collections by improving the revenue yield of ... officers;
- . self assessment was not an exercise in cost cutting - it was concerned with a redistribution of the resources to more efficiently and effectively achieve corporate objectives but a reduction in return processing was realised - mainly associated with a reduction in revenue workflows; and
- . a major benefit to the ATO was the role self assessment played in enabling, facilitating or driving other improvement initiatives, for example, Office Modernisation, [and the Electronic Lodgement Service].¹⁷

4.18 The Committee did not evaluate these contentions in detail. However it noted two points. Firstly, many factors other than self assessment could have explained the increased revenue returns to the ATO in the second half of the 1980s,

14. Evidence, vol. 18, p. S4304.

15. Evidence, vol. 4, p. S783.

16. Evidence, vol. 4, p. S976.

17. Evidence, vol. 4, pp. S974-6.

particularly economic growth. Secondly, the evaluation failed to consider the implications of self assessment for taxpayers.

4.19 Nevertheless, on the basis of cost efficiency alone the Committee concluded that it was unlikely that a return to a system of ATO assessment could be justified in terms of the consequences for revenue. However, the Committee considered that two principal aspects of the self assessment taxation system needed to be evaluated. They were:

- . the potential for income to be understated and expenses overstated because of taxpayer assessment; and
- . the public perception that the opportunity to evade tax was increased because of self assessment.

4.20 Evidence presented to the Committee demonstrated that it was not economical for the ATO to seek to collect every possible cent of revenue under either assessment system. Resource scarcity required that arbitrary thresholds for assessment or review action needed to be established. In the area of PAYE taxpayers, such thresholds can be determined by analysis of the potential revenue foregone from various aspects of the revenue collection system.

4.21 The ATO advised the Committee that in 1990-91 52% of PAYE taxpayers claimed work related expenses of less than \$300. In addition, 87% of PAYE taxpayers declared interest income of less than \$500.¹⁸ While it is possible that a proportion of the 87% of PAYE taxpayers who declared interest income of less than \$500 actually earned in excess of this amount, such a statistic demonstrates that the extent of the revenue at risk in the PAYE area is probably of such a level as to warrant the continued use of strategic approaches rather than the adoption of a comprehensive assessment system. The potential revenue gains from thorough assessment would in all probability not exceed the cost of maintaining such an assessment system.

4.22 Cognisant of the use of thresholds within the previous ATO assessment system,¹⁹ the Committee considered such limits to be sensible, provided they were monitored and amended as necessary. It was recognised that the use of thresholds may lead to a reduction in declared income or overstatement of eligible expenses, thus resulting in losses in potential revenue. However, the alternative of absolute scrutiny could not be justified on cost grounds alone.

18. Evidence, vol. 16, p. S3287.

19. *ibid.*

4.23 The ATO agreed that public knowledge of its use of thresholds provided the potential for some taxpayers to risk the chances of detection. In considering this proposition the Committee recognised that the potential for evaders to make these calculated assessments existed regardless of which entity performed the taxation assessment function. Self assessment as a system of collection, relies upon audit activity as the principal vehicle for detecting fraud. To be effective this audit function must be supported by a systematic evaluation of both risk and probability. In its evidence to the Committee the ATO stressed these two factors as integral to a successful audit strategy.

4.24 At the commencement of the self assessment system, the ATO established the goal of a 2% audit coverage of the taxpayer population by 1992. Evidence to the Committee suggested this target had been exceeded.²⁰ More importantly, audit coverage had been targeted in such a manner as to capture the maximum revenue, utilising a given audit resource. Hence audit coverage of certain sectors of the taxpaying community significantly exceeded the 2% target while total coverage of the entire population was less than 2%.²¹

4.25 The Committee formed the view that, when considered in terms of cost efficiency for the ATO, a self assessment system could be considered to be superior to pure assessment by ATO assessors. However, in the absence of evidence of taxpayer behaviour and response to the two alternative systems, such a conclusion for the entire community could not be absolutely determined.

4.26 Similarly, claims of improved voluntary compliance arising from self assessment²² could not be absolutely confirmed by the Committee in the absence of evidence of the level of compliance prior to the introduction of self assessment. While it was not possible to determine that self assessment had not led to a reduction in the level of taxpayer compliance, it was clear to the Committee, on the basis of the evidence presented to it, that there were distinctly contradictory opinions regarding the possible or potential revenue implications flowing directly from the utilisation of a self assessment system.²³

4.27 In considering the effectiveness of a self assessment system, it is necessary to construct a measure of effectiveness which takes into account all the elements of the taxation system. To this end, it must be remembered that the self assessment system is yet to be extended to all taxpayers.

20. Evidence, vol. 4, p. S973.

21. Evidence, vol. 4, p. 1131.

22. Evidence, vol. 4, p. S974.

23. Evidence, vol. 2, p. 456; vol. 3, p. 712.

4.28 Following representations from taxpayer and tax professional representative bodies, the Government acknowledged the need to improve the self assessment system. On 13 December 1990, the Government announced its intention to make changes to the income tax law to address concerns about the operation of self assessment. The objective of the review was:

... to provide a more supportive legislative and administrative environment for existing self assessment arrangements, and in so doing to make the taxation system fairer and more certain.²⁴

4.29 A consultative document, *A Full Self Assessment System of Taxation*, was released and the Government announced the broad features of what came to be known as the Self Assessment Priority Tasks Project.

4.30 The Committee noted that the decision to review the operation of the self assessment system in 1990 specifically sought to address the problems which had been perceived to arise from grafting the self assessment administrative systems onto a legislative framework constructed to support ATO assessing.²⁵ Areas of review considered in the consultative document included:

- . penalties;
- . interest;
- . Rulings;
- . elections; and
- . record keeping.

4.31 All of these areas are discussed elsewhere in this Report. In general, the amendments introduced into law in 1992 via the *Taxation Laws Amendment (Self Assessment) Act 1992* were designed to address the legislative incompatibility of aspects of self assessment. Greater certainty under the law was one of the main objectives of the Priority Tasks Project's measures.²⁶

24. Honourable John Kerin, MP, Treasurer *Improvements to Self Assessment - Priority Tasks*, An information paper, 20 August 1991, Commonwealth of Australia, 1991, p. 2.

25. Evidence, vol. 3, p. S471; vol. 2, p. 573.

26. Hon John Kerin, Treasurer, op. cit., p. 7.

4.32 How effective self assessment proves to be as a system of revenue collection will ultimately be determined in terms of the revenue collected, the commitment of taxpayers to the system and the fairness and equity of the system. Without detailing issues discussed elsewhere in this Report, the Committee concludes that the changes introduced as a result of the Priority Tasks Project have contributed significantly to an improvement in the level of equity and fairness in the taxation system. While evidence provided by taxpayer representatives and tax professionals supports this conclusion,²⁷ the Committee reserves its judgement on the effectiveness of self assessment pending further review of the legislative framework of the *Income Tax Assessment Act 1936* and the full implementation and testing of the changes introduced as a result of the Self Assessment Priority Tasks Project.

Costs of Compliance

4.33 As noted earlier, the Committee was concerned at the apparent lack of consideration which had been accorded formally to the implications of self assessment on taxpayers. Evidence highlighted the increased responsibilities and costs imposed on taxpayers and their agents by self assessment.²⁸

4.34 For individual taxpayers, compliance costs in respect of new taxing activity can potentially exceed the total revenue returned to the Commonwealth, although over time there will generally be a diminishing marginal cost of compliance, all other things being equal.

4.35 To date, it has not been a requirement that the cost of compliance be calculated or estimated prior to a legislative change being enacted. As the law has been adjusted on a piecemeal basis, compliance costs have not been viewed as a necessary concern for the revenue. To the extent that the Commonwealth does not pay tax, compliance costs have not been a major consideration in making legislative change. However, compliance costs do affect the capacity of business to function profitably. Moreover, the greater the cost of compliance the greater the incentive for taxpayers not to comply. Compliance costs can therefore be considered to include the additional costs arising from obscure, complex or uncertain law. While it is difficult to calculate the cost of complying to any given law for any given taxpayer, it is reasonable to consider compliance costs as a factor in the efficiency of an economy - though not necessarily one which is of itself critical.²⁹

27. Evidence, vol. 3, pp. S467, S574.

28. Evidence, vol. 6, p. S884; vol. 1, p. 192.

29. Evidence, vol. 2, p. S123.

4.36 In the Committee's opinion the proposition that taxpayers were being forced to consult professional help more consistently was significant.³⁰ The Committee noted the availability of free advice provided by the ATO but also noted criticisms of both the quality of advice,³¹ the ease of access to the service³² and the speed of response.³³ In the Committee's view, the root problem lay in the necessary assumptions of a self assessment system; that all taxpayers understand and have the capacity to apply the law. Under the current framework this cannot be assumed.

4.37 The Committee recognised that failure of perfect knowledge was an impediment to the efficiency of a self assessment system.³⁴ In the Committee's view such an obstacle must be readily acknowledged and catered for in the system's design. The Committee noted the changes in the penalty structures introduced as a result of the Self Assessment Priority Tasks Project and in particular, the use of tests of reasonableness.³⁵ The Committee welcomes these developments as an acknowledgment of the need to being a balance of reality to the self assessment system. Further comment on these changes is contained in Chapter 12.

4.38 As lawyers, accountants and tax agents are being required to take a more prominent role in the affairs of average taxpayers,³⁶ there is an increased cost of compliance within the system as a whole. While taxpayers have always been required to maintain and report their taxation affairs in such a manner as to enable a calculation of a tax liability, the increased complexity of the law, when taken together with a self assessment system, has in the Committee's view increased compliance costs.

4.39 The Committee considered evidence of increased taxpayer utilisation of professional services indicated fundamental inefficiencies in the structure and operation of the taxation system and concluded that the responsibility for establishing commitment and understanding of the taxation laws rested with the ATO.

4.40 The Committee regards it as the duty of the ATO to provide the necessary information to taxpayers to enable them to comply with the law. To this end the Committee regards the further development and distribution of targeted information brochures and pamphlets for specific taxpayer groups to be both

30. Evidence, vol. 3, p. S398; vol. 4, p. S884.

31. Evidence, vol. 3, p. S474.

32. Evidence, vol. 3, p. S473; vol. 4, p. S878.

33. Evidence, vol. 7, p. S1134.

34. Evidence, vol. 14, p. S2783.

35. *Taxation Laws Amendment (Self Assessment) Act 1992*.

36. Evidence, vol. 2, p. 575.

innovative and efficient. Such a program, however, should not be at the expense of a fundamental commitment to rewriting the taxation law.

4.41 Self assessment has drawn into sharp relief the role of professional advisers.³⁷ Not only are more taxpayers seeking professional advice but the knowledge required of advisers has become more extensive and technical. This has led to increased pressure being placed on tax agents, particularly the smaller agents. The risk of not seeking advice for a taxpayer may even be a breach of the 'reasonable' tests under the self assessment penalty regime. Thus, the cost of both direct advice and uncertainty has increased to taxpayers. The spectre of professional negligence is also intensified as a result of greater legislative complexity and larger client numbers.

Proposals to Extend Self Assessment

4.42 Self assessment in its fullest form is yet to be extended to all taxpayers.³⁸ While appreciating the ATO's commitment to self assessment,³⁹ the Committee considers that the implications for individual taxpayers, as well as the possible revenue implications and economic costs, of an extension of self assessment requires that further discussion and evaluation be conducted prior to proceeding to full implementation. In particular, the Committee notes the urgent need to review the legislative base for self assessment within the taxation system. This matter is considered in detail in Chapter 5.

4.43 The Committee is of the view that if self assessment is to be a valid administrative system, taxpayers should be able to broadly understand their taxation obligations by reference to the relevant provisions of the Act without excessive need for professional advice. Such issues were identified by witnesses from the ATO before the Committee.⁴⁰ Moreover, the Committee considers it to be imperative that an agreed legislative framework to support a full self assessment system should be in place prior to the system's extension to the general taxpayer. Furthermore, properly documented administrative guidelines, in plain English, need to be developed and made available to the public before self assessment is generally extended.

37. Evidence, vol. 15, p. S3012.

38. Evidence, vol. 4, p. S981.

39. Evidence, vol. 5, p. 1526.

40. Evidence, vol. 1, pp. 22-4.

4.44 Given the complexity of Australian tax law the Committee recommends that:

- . the further extension of the self assessment system be delayed pending the development of a comprehensive supporting legislative framework; and
- . the Australian Taxation Office develop and make publicly available appropriate information for taxpayers on their obligations under a self assessment system.

4.45 The Committee envisages that the availability of documentation which provides taxpayers with information on their taxation liabilities under a self assessment system will both increase taxpayer compliance and reduce the cost to taxpayers of preparing return forms. Indeed the Committee noted that, with the future extension of full self assessment to PAYE taxpayers, an opportunity would exist to provide PAYE taxpayers with an option to lodge returns.

4.46 This situation would eventuate as a result of the continued restriction of deductible work related expenses and the ATO's further development of income monitoring systems. Through comparing the costs to both the PAYE taxpayer and the ATO in the preparation, lodgement and processing of PAYE returns with the limited net return from this procedure, the Committee concluded that the investigation of an optional return system should be further advanced by the ATO. Such an evaluation should be conducted in association with proposals for the extension of the self assessment system.

4.47 The Committee noted that the ATO had already given some consideration to proposals to remove the need for lodgement of returns by some PAYE taxpayers.⁴¹ As stated by the ATO, and acknowledged by the Committee, these proposals can best be considered in the context of legislative simplification. This crucial issue is discussed in the following chapter.

41. Evidence, vol. 10, p. S1597.

Chapter 5

LEGISLATIVE FRAMEWORK

- . Introduction
- . Problems with the Current Act
- . Administering the Unadministerable
- . Self Assessment
- . Costs of Compliance
- . Rewriting the Act
- . Legislative Drafting Process
- . Proposals for Change

Introduction

5.1 The *Income Tax Assessment Act 1936* (the Act) is the principal taxation Act in Australia. It has been kindly described as cumbersome and idiosyncratic.¹ When first passed by the Commonwealth Parliament and given Royal Assent, the Act covered just 126 pages.² The evidence presented to the Committee suggested the Act and its associated material has grown to over 5 000 pages.³ While the absolute size of the Act is not of critical importance, the impact of its provisions on the functioning of the Australian economy cannot be underestimated.

5.2 The Committee's Terms of Reference did not include an examination of the merits of the Act, but it was patently clear to the Committee from an early stage, that the efficiency of the administration of the income tax system by the Australian Taxation Office (ATO) was inexorably linked to the inherent efficiency of the Act as a legislative instrument. Submissions from a wide cross section of the community invariably urged the Committee to consider the merit of the current Act.⁴

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1. *Butterworths Australian Tax Legislation 1992, vol. 1, Income Tax Assessment Act*, Butterworths Pty Ltd, 1992, p. vi.
 2. Evidence, vol 1, p. 30.
 3. Evidence, vol 1, p. 30.
 4. Evidence, vol. 1, pp. S3, S58; vol. 2, p. S109; vol. 3, pp. S349, S606; vol. 5, pp. S703, S725.

5.3 In view of the Inquiry's terms of reference the Committee did not seek to examine the mix of taxation or the general content of the Act but examined and considered the effect the current legislation had on the efficiency of the taxation system. Moreover, the Committee considered the process which had led to, and continues to contribute to, the Act's inappropriate style and composition.

5.4 Also outside the Committee's terms of reference was consideration of the merit of taxing income as a source of revenue. Therefore while the Committee noted the difficulties which had arisen as a result of the need to define income and distinguish income from capital, it did not consider alternatives to the income tax system.⁵

Problems with the Current Act

Complexity

5.5 Much evidence suggested that the complexity of the Act was the principal, underlying problem of the current taxation system.⁶ This can be considered to derive from two interrelated factors. The first is the general complexity of current life, in particular, commercial life. The second factor is the attempt by successive governments to circumvent possible evasion practices through the drafting of comprehensive legislation. The fact that the Act is also used extensively as an instrument to deliver government policy outcomes, such as gift provisions and investment allowance, is also seen as a contributing factor. A former Commissioner of Taxation has proposed five factors, which more definitively explain the law's complexity. They are:

- . the difficulty of establishing a definition of income;
- . the matters the law seeks to deal with are complex;
- . the need to build qualifications and exceptions into the law;
- . difficulties in defining the boundaries of particular provisions;
and

5. For a definition of 'Income' see Ross S, Burgess P, *Income Tax - a Critical Analysis*, The Law Book Company 1991, p. 31; for the problem of income capital distinction see Evidence, vol. 2, pp. S152-3.

6. Evidence, vol. 3, p. S477; vol. 5, p. S730; vol. 6, p. S893; vol. 7, pp. S1070, S1154; vol. 18, p. S4319.

the need to respond to judicial authorities which have provided a literal approach to statutory interpretation.⁷

5.6 While not necessarily agreeing that these are all of the factors, the Committee acknowledged the extent to which each factor had contributed to the complexity of the Act.

Uncertainty

5.7 Uncertainty of the Act's application to particular or even general circumstances was considered by the Committee to be a factor adding to the costs of administering the taxation system both for taxpayers and the ATO. The Committee was aware of the importance of certainty to taxpayers and in particular, corporate taxpayers. As a representative of the Business Council of Australia stated:

... what business wants out of its tax law is both that it should impact fairly upon all enterprises and that there should be certainty in outcomes.⁸

5.8 The Committee noted that achieving certainty of outcome from a piece of legislative folklore, in a rapidly changing world, was not an easy objective. Furthermore, given the capacity of commercial transactions to deliver previously unheard of outcomes, uncertainty of the taxation obligation could be considered inevitable. The Committee considered uncertainty was not of itself an outcome which could be blamed on the Act, in all cases. The existence of seemingly divergent schools of thought on the merit of black letter law (that is, law which is drafted in great detail so as to indicate its application in every possible circumstance)⁹ versus the use of statements of general principle, commonly referred to as fuzzy law, indicated to the Committee that the existence of uncertainty in the Act would not easily be removed merely through a change to the style of legislative drafting.

7. Evidence, vol. 18, pp. 4319-21.

8. Evidence, vol. 1, p. 280.

9. House of Representatives Standing Committee on Legal and Constitutional Affairs, *Clearer Commonwealth Law*, AGPS, Canberra, September 1993, p. 213.

Problem of Expression

5.9 During the Inquiry, numerous witnesses urged the redrafting of the Act in plain English. This request principally sought to address the need for taxpayers, in a self assessment environment, to understand and comprehend tax law. The form and style of the Act is patently legalistic and as such it limits the number of people, both taxpayers and officers of the ATO, who can understand the nuances of the law. As one witness remarked, 'the law has become so difficult to access and to understand that it is virtually incomprehensible to the lay or even the educated lawyer'.¹⁰ The style of drafting was considered by this witness to be less important than the method of expression; 'it is a fact that [by] the way the law has been drafted we certainly have, in a sense, black-letter law, but it is black-letter law that cannot be understood.'¹¹

5.10 Plain English was defined by Mr David St Ledger Kelly, Chairman of the former Law Reform Commission of Victoria, in the following manner:

... it is just accurate, simple English, which in the context of legislation and in the context of rewriting an Act means no more than getting rid of overlay of language which a legalistic style has imposed upon the Tax Act. In other words, plain English is not something that exists in itself; it is just getting rid of unnecessary legalese, unnecessary language, unnecessary distortion, bad structure, incoherence in the form in which things are put, it is getting rid of bad things about legislation and keeping everything that is good and necessary.¹²

5.11 Evidence presented to the Committee indicated that significant benefits would arise from a redraft of the Act in plain English.¹³ Perhaps more important was the suggestion that a rewrite would allow for ready comprehension of the Act by a large part of the community.¹⁴ Furthermore, a plain English redraft could incorporate all complex concepts, particularly those which had been given judicial interpretation.¹⁵

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10. Evidence, vol. 1, p. 288.
 11. Evidence, vol. 1, p. 284.
 12. Evidence, vol. 2, p. 388.
 13. Evidence, vol. 2, p. 387.
 14. Evidence, vol. 9, p. S1402.
 15. Evidence, vol. 2, p. 389.

5.12 The Committee agreed with one witness who argued that it was not necessary for the taxpayers to understand every concept in the Act but it was critical that those parts of the Act which affected the majority of the community should be unravelled and explained more clearly.¹⁶

Administering the Unadministerable

5.13 A good law can be measured in part by its capacity to be administered. Where a law cannot be administered or the administration of the law fails to achieve the stated aim of the law, then the integrity of the underlying policy may be eroded.

5.14 The Committee received evidence from ATO auditors about difficulties that they had experienced in administering certain provisions of the Act and in particular, s. 128F.¹⁷ This evidence demonstrated to the Committee the problems that can result from a division of responsibilities in the drafting and preparation of legislation in so far as implementing a policy is concerned.

5.15 In essence, s. 128F provides for a withholding tax exemption on interest paid on Australian business borrowings to non-residents in respect of widely held debentures. To be eligible for the s. 128F debenture exemption certain criteria must be satisfied. The criteria contained in s. 128F requires, in part, that these debentures must be issued with a view to wide distribution.

5.16 Given the nature of the requirements that must be satisfied under s. 128F of the Act, particularly in relation to wide distribution, it is often difficult for branch offices of the ATO to be fully satisfied that these requirements will be fully complied with. This may lead, on occasions, to perceived inconsistencies in application approvals. On the other hand, industry requires a uniform and consistent approach to the approval of s. 128F applications. The absence of such an approach can lead to potential market uncertainty and instability. These problems arise primarily from the conflict between the ATO's reluctance to grant approval where not fully satisfied that all s. 128F requirements will be complied with, and the perception from industry that the approval process is inconsistent.

16. Evidence, vol. 9, p. S1402.

17. Evidence, vol. 4, p. 1089.

5.17 Evidence from ATO auditors referred to the difficulties they had experienced in administering s. 128F. In their view it provided an opportunity for tax evasion.¹⁸ The ATO acknowledged that the s. 128F exemption needed to be safeguarded against tax avoidance.¹⁹

5.18 Income Tax Ruling IT 2647 provides that undertakings given by banks and other financial institutions regarding the use of funds exempted under s. 128F are sufficient to satisfy the requirements of the section. While such undertakings are an administrative necessity, the position of auditors in such circumstances is untenable. Their capacity to supervise this particular section is severely limited by the application of Rulings. However, the essential nature of the law has not changed and in effect the ATO has circumvented a difficult to administer provision by administrative means. In the Committee's view the ATO's pragmatism, while possibly commendable, does not advance respect for the law.

5.19 **Consequently the Committee recommends that:**

the Government introduce legislation to amend Section 128F of the *Income Tax Assessment Act 1936* to clarify its meaning and application.

Self Assessment

5.20 In the Committee's view the introduction of self assessment has increased the importance of an efficient legislative framework. This is particularly so because of the presumption within a self assessment system of the capacity of taxpayers to interpret and apply the law. While fairness dictates that taxpayers should not be penalised because of a failure in the basic tool of the self assessment system,²⁰ evidence indicated that the burden on taxpayers and the potential for the imposition of penalties had increased as a result of self assessment.²¹

5.21 The Committee concluded that the self assessment system had been grafted upon an already unstable legislative base and as such had increased the cost to taxpayers of complying with the law. More significantly, the legislative base for self assessment had not been full amended to take account of the requirement of administration and the rights of taxpayers.²²

18. Evidence, vol. 4, pp. 1089-95.

19. Evidence, vol. 18, p. S4126.

20. Evidence, vol. 9, p. S1401.

21. Evidence, vol. 3, p. S398; vol. 6, p. S884; vol. 7, p. S1056.

22. This matter is considered more fully in Chapter 4.

Cost of Compliance

5.22 As indicated in Chapter 4, the Committee noted the increased cost of compliance which had fallen upon taxpayers as a result of self assessment not being introduced in conjunction with a fundamental adjustment to the legislative framework of the Act. The Committee concluded that maximum efficiency in a self assessment system could only be achieved after a rewriting and recasting of the Act.

5.23 As an example of the importance of the recasting, the Committee noted the continued existence of extensive discretions in the province of the Commissioner of Taxation. Such discretions were considered by witnesses to be contrary to a self assessment philosophy and the Committee concurs with this point of view.²³

Rewriting the Act

5.24 A former Commissioner of Taxation has stated, "The Parliament cannot expect the general public to observe a tax law that it cannot readily understand."²⁴ If this is right, then the recent comments of the Chief Justice of the High Court of Australia would suggest that the Parliament cannot expect taxpayers to generally observe at least certain provisions of the Capital Gains Tax sections of the Act.²⁵

5.25 During the Inquiry the ATO emphasised the need for progress in redrafting the Act:

We must do something fundamental ... To use another analogy, the snowball has been rolling down the hill for a long time now, threatening to bury us. It might not be this year or next year but we can see that in time it will happen. I believe that Australia, along with other developed countries which have much the same legislative problem, has to turn its attention to dealing really fundamentally with that issue.²⁶

23. Evidence, vol. 6, p. S996; vol. 7, p. S1068.

24. Commissioner of Taxation, *Annual Report, 1990-91*, AGPS, p. 10.

25. *Hepples v Federal Commissioner of Taxation*, 91 ATC, 4808 per Mason CJ.

26. Evidence, vol. 1, p. 31.

... there is a great deal of accord in the community, including in the Tax Office, that the situation cannot really continue on without something needing to be done to try to make the law a little less complex and easier to work with than it currently is.²⁷

5.26 The Committee noted that while some thinking was occurring within the ATO as to how best to carry out a legislative redraft,²⁸ the ATO had not advanced very far in its thinking. The Committee also noted taxpayer criticism of the ATO's commitment to simplification of the Act.²⁹

5.27 It was suggested during the Inquiry that simplicity may sometimes come at the cost of equity, particularly in an income tax system which was structured to balance equity, efficiency and simplicity.³⁰ The words of the Commissioner of Taxation in 1926 ably summarise this:

... It is truism that equity cannot be secured in taxation laws without complexity. Complex law involves forms of return for income, and the complicated forms give rise to demands for simplification of the law.³¹

5.28 The Committee is of the view, that any attempt to redraft the Act must necessarily look at broader, structural issues within the total taxation system. Simplification, in this context, should concentrate on achieving a tax system which is fair, equitable and economical. The objective must be to reduce the total cost of the taxation system. Consequently a redraft of the Act, while crucial, cannot be successfully achieved in the absence of a fundamental review of the administrative, political and social implications of changes in the Act.

27. Evidence, vol. 5, p. 1509.

28. Evidence, vol. 5, p. 1509.

29. Evidence, vol. 8, p. S1397.

30. Evidence, vol. 18, p. S4316.

31. Commissioner of Taxation, *Ninth Annual Report*, Commonwealth Government Printer, 1926, p. 3.

5.29 The Committee received evidence concerning a proposal to redraft a particular Division of the Act in a plain English style. The Committee noted the merits of such an attempt but was also cognisant of the significant difficulties raised by such an exercise. In particular, evidence from the Commonwealth's First Parliamentary Counsel highlighted the difficulties of major redrafting, particularly the importance of establishing the underlying policy of the Act and the need to maintain, where necessary, precision.³²

5.30 Consequently, in performing a redraft, the Committee believes the fundamental assumptions underlying the Act, including the basis on which the Act is to be administered and the policy decisions inherent in the Act, should be evaluated, discussed and clarified. For example, the possible alignment of the taxation law with accounting standards and concepts would be a fundamental change to be considered.

5.31 During the Inquiry the Committee noted proposals for the establishment of a specialist committee to oversee a redraft of the Act.³³ The Committee considered such a committee to be too limited given the fundamental significance of the proposal for a redraft. The Committee has concluded that a broadly based task force drawing upon a wide cross-section of skills, experience and the professions, would represent a suitable vehicle for the performance of this significant duty.

5.32 The Committee noted the proposal by the Taxation Institute of Australia for a redraft of the Act.³⁴ The Committee concurs with the sentiment inherent in the Institute's paper and agrees that the time is right for a new Act. Moreover, the Committee considers there is much merit in the Institute's proposal to separate the Act and to conduct the redraft in stages.

5.33 As discussed later in this chapter, the Committee considered there were significant economic benefits for the whole Australian economy in rewriting the Act. Such a rewrite however, would only be possible with the absolute commitment of all political parties, the bureaucracy, the taxation industry, business and taxpayers generally. To this end the Committee considered the Government needed to demonstrate its commitment by the allocation of sufficient resources to the project. The importance of this task necessitated that such a commitment be provided as soon as practicable.

32. Evidence, vol. 8, p. S1373.

33. Evidence, vol. 7, p. S1157.

34. Evidence, vol. 13, p. S2463.

5.34 One proposal that the Committee felt had certain attractions was based on the premise that simplification resources were best directed, firstly, towards ensuring simplification objectives were met in respect of all new legislative proposals and secondly, towards targeting those areas of the law which were both complex and affected a significant number of taxpayers.

5.35 The Committee's recommendations in this chapter in relation to the preparation of Taxation Impact Statements should go some way towards addressing the first objective. In relation to the second objective, the Committee felt that a degree of consensus should be able to be achieved through consultation in relation to the most important twenty-five simplification priorities selected on the basis of a complexity/significance impact test. The Committee concluded that these identified areas should form the first stage of the simplification/redraft project and that redrafting should to be completed within two years.

5.36 Fundamentally, however, the Committee felt that the redrafting priorities should be determined by the proposed task force through extensive consultation.

5.37 In the view of the Committee, the task force should be established outside the formal structures of both the ATO and the Treasury. Moreover, it is considered essential for the purposes of maintaining commitment that the task force be required to meet agreed reporting deadlines.

5.38 Consequently the Committee recommends that:

- . the Government establish a broadly based task force to redraft the *Income Tax Assessment Act 1936*, and
- . the Government commit sufficient resources to the task force as will allow it to complete a priority simplification redraft within two years and the full simplification of the Act within five years.

Legislative Drafting Process

5.39 The Committee noted comments that the current system of legislative drafting was contributing to the complexity of the Act and thus increasing the burden on taxpayers. As stated by one witness:

... we have got a system for writing legislation which results in the only people who can understand it being the people who draft it. ... So we have got a system under which legislation is being drafted for this country which is running the Tax Office - running the revenue of this country - and it is intelligible only to one or two people in the Office of Parliamentary Counsel. That is simply disastrous.³⁵

5.40 It was stated that this process had resulted in, 'a body of unintelligible law'.³⁶

5.41 The procedure for the drafting of taxation law was succinctly stated in a speech by the former Commissioner of Taxation to the Monash University Law School Foundation in 1991:

Proposals for change to the tax system are developed in the Tax Policy Division of the Treasury or, occasionally, in other Departments that wish to achieve a particular policy result by using the tax system, e.g. a tax concession for a particular industry. The role of the Taxation Office at this point is generally limited to providing advice to Treasury and the Government on the administrability and technical validity of policy proposals, based on a more detailed understanding of the operation of the tax law and especially its administration. The Taxation Office would also take a more leading role in the development of proposals to deal with the administration of the system (e.g., for the use of tax file numbers) or to counter avoidance.

35. Evidence, vol. 2, p. 373.

36. Evidence, vol. 2, p. 398.

Once a decision is taken by the Government to change the tax law it is the Taxation Office's role to implement it. In particular, this means fleshing out the structure and detail of the often very general decisions taken by the Government, obtaining such further decisions from Government as are necessary in this process.

It is then the role of the Office of Parliamentary Counsel to draft legislation from the detailed instructions provided by the Taxation Office.³⁷

5.42 Evidence presented to the Committee criticised the lack of integration between the Treasury and the ATO in the formulation and preparation of the taxation law, and the isolation of the Office of Parliamentary Counsel (OPC) from the decision making process.³⁸

5.43 The separation between the ATO and Treasury was clearly stated in a letter from the Secretary of the Treasury declining to make a submission to the Inquiry:

There has been a long-standing separation of policy and procedural matters between the Treasury and the Commissioner of Taxation, and the Treasury has not monitored nor sought to review the ATO's revenue raising procedures. Where procedural matters have arisen, we have left it to the Commissioner to directly advise Government or the Parliament as required.³⁹

5.44 This separation of policy and procedure does not necessarily mean that the Treasury and the ATO do not confer over the policy advice supplied to the Government. Indeed, as noted above, increased communication between officers of the Treasury and the ATO in respect of legislative developments has occurred in recent times. However, as a consequence of the formal separation of policy and administrative advice, the Committee considered there was a potential for administrative issues to be overlooked in the design of taxation policies. This was despite the 'close working relationship' between the ATO and the Treasury.⁴⁰

37. Evidence, vol. 18, p. S4318.

38. Evidence, vol. 3, p. S599; p. 650.

39. Evidence, vol. 21, p. S5044.

40. Treasury Portfolio, *Program Performance Statements 1993-94*, Budget Related Paper No. 7.17, p. 28.

5.45 One witness suggested that the preservation of the independence of those performing specific functions in the development of taxation law was to the detriment of an integrated process.⁴¹

5.46 With respect of the integration of the roles of the ATO and the Treasury in the development of policy to law, the Committee considered the independence of the ATO was worth preserving if only to distinguish between the administrative advice of the ATO and legal/political/economic advice of the Treasury. Recent efforts to improve liaison and consultation between the two organisations were noted by the Committee. The Committee considered formal liaison and co-operation between the Treasury and the ATO was crucial to the development of good legislation.

5.47 The Committee noted the formal procedures for liaison between briefing agencies and the OPC which are contained in guidelines prepared and distributed by the Department of the Prime Minister and Cabinet. The Committee considered the efficiency and professionalism of this arrangement could only be judged in the quality of the end product and any time delays in having basic legislation prepared.

5.48 Once bills have been prepared and approved by the Government, they are submitted to the Parliament. Parliamentary scrutiny of taxation bills can vary depending upon the other matters before the Parliament. Members of the Committee considered it desirable that the greatest amount of time possible should be allocated to consideration of taxation bills. However, given the significance of taxation bills to the Government's economic management framework, the Committee acknowledged the need for the Government to limit debate on taxation bills at certain times. While this outcome was considered less than optimal, it was nevertheless recognised as inevitable.

5.49 The Committee also acknowledged that flexibility in the determination and announcement of economic policy was a right of government. While the Committee recognised the advantage of fully discussed and considered legislation being brought before the Parliament, it conceded that the option of 'legislation by press release', or other administrative means, was one which all governments would exercise, though as an exception rather than as a rule.

41. Evidence, vol. 3, p. S602.

5.50 The Committee considers that the release of legislation by administrative means, such as by press release, is a highly undesirable practice. Where it occurs, the Commissioner of Taxation, should be required to provide significant details of the legislation at the time of the announcement so as to minimus uncertainty. The government of the day should then commit itself to the introduction of legislation within six months of the announcement or before the end of the relevant tax year. The Committee notes the importance of ensuring that the final legislative enactment is in line with the original announcements.

5.51 **The Committee recommends that:**

where legislation is foreshadowed in an administrative announcement, the Commissioner of Taxation be required to release significant details of the proposed legislation and the Government commit itself to the introduction of enabling legislation within six months of the announcement or before the end of the relevant taxation year, which ever is the sooner.

Proposals for Change

5.52 Suggestions for improvement in the manner by which legislation is drafted concentrated on two primary features: the structural arrangements for legislative drafting; and the involvement of the community in the policy and administration of the taxation system.

5.53 While the Committee considered the independence of the roles of the Treasury and the ATO should be maintained, it was of the view that a greater integration of the policy, drafting and administrative functions was a worthwhile goal.

5.54 The Committee concluded that two significant variations to the current arrangements would facilitate the preparation of better taxation legislation:

the integration of economic and administrative policy advice;
and

the integration of legislative drafting expertise within the ATO.

Economic and Administrative Policy Integration

5.55 It would seem incomprehensible that any policy advice to government would be provided without advice as to how the policy could be implemented. However, given the fractious nature of the Act, the Committee considered there was sufficient evidence to suggest that such a process had occurred in the past in relation to taxation issues. The Committee formed the view that to ensure this could never be the case in the future, the working relationships between the ATO and the Treasury needed to be strengthened and the relationship between these two bodies and Parliamentary Counsel redefined.

5.56 The Committee has concluded that policy advice provided to Government in taxation matters which involves amendments to the law should always present both the economic and administrative issues pertaining to any given matter. In particular, the cost of administrative compliance, to all relevant parties, including both direct and indirect costs, should be relevant considerations for any government contemplating legislative change.

5.57 With respect to any new proposals for change to the taxation law, the Committee concluded that formal policy submissions to Cabinet should be supported by the presentation of a Taxation Administration Brief, prepared by the ATO. Such a brief should set out the administrative implications of the proposed policy including a statement of the means by which the policy would be implemented and any difficulties the ATO perceived in linking the proposal within current administrative systems. Ideally, such a brief should be presented to the government as an attachment to the original policy brief.

5.58 **The Committee recommends that:**

a Taxation Administration Brief prepared by the Australian Taxation Office be submitted by the Treasurer to the Cabinet setting out the administration implications of each policy proposal involving amendments to any Act under the administration of the Commissioner of Taxation.

Tax Impact Statement

5.59 All taxation legislation is designed to impact on taxpayer groups to varying degrees and to raise revenue from, and influence the economic behaviour of, particular taxpayers. In the Committee's opinion such impacts should be evaluated and assessed by Cabinet prior to legislation being passed by the Parliament. The impacts should be identified and quantified in Taxation Impact Statements. These statements should be prepared by the ATO and tabled with explanatory memoranda.

5.60 While such things are clearly difficult to quantify, the Committee noted with concern the apparent high cost of compliance in Australia compared, for example, with the UK. A 1991 study by the Australian Tax Research Foundation (ATRF)⁴² put the total cost of compliance of public companies in Australia for the 1986-87 tax year at between \$646 million and \$1 341 billion, or between 11.4% and 23.7% of public companies' tax revenue. These figures, exclude the ATO's costs of collection and the costs of collecting PAYE and Sales Tax, but the costs of using professional help are included. The Committee could see no reason why this situation would have improved materially since the 1986-87 tax year.

5.61 A study on the compliance costs for personal income tax in Australia in 1990,⁴³ put the cost of compliance for individuals at between 7.9% and 10.8% of tax revenue or about \$4 billion. Again, ATO costs of collection were excluded and professional costs included in these figures.

5.62 The limited material available suggests that the costs of compliance in the UK to the corporate sector may be around 2.2%.⁴⁴ The Australian estimate is therefore between five and eleven times greater than that of the UK.

5.63 The Committee noted evidence that cast doubt on the quantum of costs identified in the ATRF 1991 study.⁴⁵ Nevertheless, using the above details and taking into account ATO costs, it may well be that the total cost of compliance in Australia is between 10% and 15% of tax collected or between \$7.5 billion and \$11 billion. Even if such an estimate was excessive by say a factor of two, a 10% simplification saving dividend would yield an annual economic benefit/cost saving

42. Pope J, Fayle R, Chen D-L, *The Compliance Costs of Public Companies' Income Taxation in Australia, 1986/87*, Australian Tax Research Foundation, Sydney, 1991.

43. Pope J, Fayle R, Duncanson M, *The Compliance Costs of Personal Income Taxation in Australia*, Australian Tax Research Foundation, Sydney, 1990.

44. Pope J, Fayle R, Chen D-L, op. cit., p.18.

45. Evidence, vol. 1, p. 128.

to the Australian economy of some \$500 million. Evidence from one witness agreed that the saving to the Australian economy of a simplification of the Act would be in the order of \$180 million to \$330 million per annum.⁴⁶

5.64 The Preface to the ATRF 1991 study stated:

The researchers recognise that the Commissioner of Taxation has a statutory duty to administer the laws imposed by Parliament and is not a law maker. Improvement to the administration of the income tax system is largely dependent upon the laws. It is the latter which must be addressed if reform is to facilitate a cost efficient system in terms of both government administration and taxpayer compliance.⁴⁷

5.65 To quote further from the Foreword of the study:

It seems reasonable to conclude that Australian companies are subject to a hidden, but substantial, burden in the form of excessive compliance costs. The elimination of the excessive component of these costs via tax simplification is urgently required.⁴⁸

5.66 The Committee concludes that the cost of compliance needs to be explicitly recognised whenever new legislation is prepared. There is little point in simplifying the Act if in the meantime the cost of complying with new legislative provisions increases the economic inefficiency of the current Act.

5.67 **The Committee recommends that:**

all future taxation legislation be supported by a Taxation Impact Statement which details the impact on taxpayers of the legislation, including the total compliance cost and the extent to which simplification objectives have been achieved.

46. Evidence, vol. 2, p. 387.

47. Pope J, Fayle R, Chen D-L, op. cit.

48. *ibid.*

5.68 The Committee noted that the UK had introduced a system involving Compliance Cost Assessments (CCA). CCA are structured appraisals that all UK Government departments must prepare when evaluating policy proposals likely to affect business. Their stated purpose is to inform business and officials of the likely costs to business of complying with new or amended provisions so that compliance costs can be assessed and any unnecessary burden to business identified well before a decision is taken on whether or not to go ahead with the proposals. The Committee believes that the CCA system provides a model upon which an Australian Taxation Impact Statement system could be based.

5.69 Taxation Impact Statements should include all assumptions used by the ATO and the Treasury in determining a tax's relative burden. In particular they should include an identification of the consequences for international competitiveness.

Parliamentary Counsel

5.70 The establishment of a separate agency responsible for legislative drafting provides the Commonwealth with the capacity to ensure consistency of drafting style. While this style may be the subject of critical comment, consistency of style has certainly been achieved.⁴⁹ However, the objective of consistency should not be allowed to override the more important objective of the preparation of legislation which is comprehensible for the average citizen. In the Committee's view, elite law is bad law.

5.71 To ensure the legislative drafting of taxation law does not produce an elite text of provisions, the Committee believes more integration of the roles of instruction and drafting is required. To this end, the Committee considers officers of the OPC should be permanently situated within the central office of the ATO. Moreover, the formal processes of instruction should, to the extent considered appropriate, be abandoned and a more flexible arrangement introduced, which includes greater oral communication. Such a process should involve Parliamentary Counsel, where appropriate, in interaction and liaison with industry groups and professional associations.

49. Evidence, vol. 2, p. 386.

5.72

The Committee therefore recommends that:

- officers of the Office of Parliamentary Counsel responsible for the drafting of taxation legislation be located in the Australian Taxation Office for the purpose of drafting taxation legislation.**

5.73

In making this recommendation the Committee recognises the need for these officers to remain employees of the OPC and for such officers to be rotated through the ATO as and when considered appropriate by the First Parliamentary Counsel.

