COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

ECONOMICS REFERENCES COMMITTEE

Reference: Operations of the Australian Taxation Office

TUESDAY, 14 SEPTEMBER 1999

MELBOURNE

BY AUTHORITY OF THE SENATE

INTERNET

The Proof and Official Hansard transcripts of Senate committee hearings, some House of Representatives committee hearings and some joint committee hearings are available on the Internet. Some House of Representatives committees and some joint committees make available only Official Hansard transcripts.

The Internet address is: **http://www.aph.gov.au/hansard**

To search the parliamentary database, go to: **http://search.aph.gov.au**

SENATE

ECONOMICS REFERENCES COMMITTEE

Tuesday, 14 September 1999

Members: Senator Murphy *(Chair)*, Senators Chapman, Conroy, Cook, Gibson and Murray

Substitute members: Senator Sherry for Senator Cook

Participating members: Senators Abetz, Boswell, Brown, Brownhill, Calvert, George Campbell, Coonan, Crane, Eggleston, Faulkner, Ferguson, Ferris, Harradine, Knowles, Lightfoot, Mason, McGauran, Parer, Payne, Quirke, Ridgeway, Tchen, Tierney and Watson

Senators in attendance: Senators Chapman, Murphy, Sherry, Stott Despoja and Watson

Terms of reference for the inquiry:

Matter referred by the Senate for inquiry into and report on:

(a) the equitable treatment of taxpayers;

(b) the performance of the Large Business and International Division, including, in particular, the High Wealth Individual Project;

(c) compliance by the ATO with the Client Settlement Guidelines; and

(d) allegations of infiltration of the ATO by organised crime.

WITNESSES

Committee met at 9.19 a.m.

CHAIR—Today the committee will continue its inquiry into the operation of the Australian Taxation Office. The terms of reference for the inquiry direct the committee to consider the operation of the ATO with particular reference to the equitable treatment of taxpayers; the performance of the Large Business and International Division including, in particular, the high wealth individuals project; compliance by the ATO with the client settlement guidelines; and allegations of infiltration of the ATO by organised crime.

Before we commence taking evidence, I wish to state for the record that all witnesses appearing before the committee are protected by parliamentary privilege with respect to evidence provided. Parliamentary privilege refers to special rights and immunities attached to the parliament or its members and others necessary for the discharge of the parliamentary functions without obstruction and fear of prosecution. Any act by any person which operates to disadvantage a witness on account of the evidence given by him or her before the Senate or any of its committees is treated as a breach of privilege.

I wish to stress that the interference with a witness may involve seeking to influence witnesses in respect of evidence they may give, or inflicting penalty or injury on witnesses in consequence of their evidence. Both kinds of interference would constitute a contempt of the Senate for which the Senate has the power to impose penalties. I would also like to make it clear that the Senate takes these protection mechanisms very seriously and will vigorously pursue any breach of privilege. The committee prefers all evidence to be given in public, but under the Senate's resolutions witnesses have a right to request to be heard in private session.

Evidence was then taken in camera, but later resumed in public—

[10.33 a.m.]

GIRDLER, Mr Paul Howard, Section Industrial Officer, Tax Section, Community and Public Sector Union

O'CONNELL, Mr Shane Patrick, Secretary, Tax Section, Community and Public Sector Union

GUTHREY, Mr David Lloyd, Section Counsellor, CPSU Tax Section, Australian Taxation Office

CHAIR—Welcome. The committee prefers all evidence to be given in public, but under the Senate's resolutions you have the right to request to be heard in private session. Before we proceed, may I also draw to your attention the nature of this and other Senate committee inquiries. Senate committees do not have the power to make the determinations or orders and do not have a function as a dispute resolution body.

Without pre-empting the committee, I point out that based on past practices it is unlikely that the committee will make recommendations on individual cases. Rather, it is expected that the committee will explore a number of individual case studies in order to draw a conclusion on general or systemic issues in the operation of the Australian Taxation Office. Because of this, as far as possible the committee wishes to avoid receiving evidence that constitutes adverse comment about individuals. If you wish to refer to an individual adversely, you should be aware that the committee is obliged to extend a right of reply, so you should wherever possible refer to individuals as 'Mr X', et cetera, but if you do wish to refer to an individual by name I would request that you advise us. That will enable us to make a determination as to whether we want to proceed into private session. I now invite you to make an opening statement.

Mr O'Connell—Thank you. The CPSU is very grateful to be able to present a submission to this committee. We believe it is an important committee in terms of the administration of the ATO. The terms of reference of the committee touch on four areas. We want to focus primarily on one of those, which is the equitable treatment of taxpayers, as the administration of the ATO feeds into that particular one. We have less to say about the performance of the Large Business and International Division, the compliance by the ATO with the client settlement guidelines, and allegations of infiltration of the ATO by organised crime. On the latter we would simply leave it on the basis that there is not much evidence, to our knowledge, of that fourth area. Others will undoubtedly make submissions about those particular areas. What we would like to do is provide some background information that will assist the committee in terms of its deliberations and, particularly after having heard other submissions, this might add up to a picture that the committee are then able to put together.

We come here obviously on behalf of the majority of staff of the ATO, who have a wide range of concerns about the administration of the ATO. The ATO, as we all know, is a very significant organisation in the Australian community, collecting over $140 billion, estimated to go up to $147 billion, and of course it is now at the commencement of a process of introducing a new tax system, including a GST. We come here on behalf of the 15,000 dedicated ATO staff, who face enormous resistance at times to the performance of their

duties in terms of very powerful elements in the community who would like to minimise their taxation, but also, to summarise it, they feel that they are not receiving the required support from their leadership.

The Commissioner is a very powerful public figure, as you are well aware, in terms of being in charge of an organisation collecting over $140 billion. The Commissioner also has a seven-year term of office, of which you are undoubtedly also aware, and can only be removed by, I believe, a common motion going to both houses of parliament during the same session. So the Commissioner is a very powerful public servant in the capacity of this country. We therefore believe that in terms of the administration of the ATO, given the particular power vested in that individual, there need to be checks and balances in the system in terms of general administration, in terms of settlements and compliance—and our members have raised concerns about the way settlements are conducted; in terms of the delivery of service to the community; the prevention of criminals and other undesirable elements being employed by the ATO; the expenditure of government dollars, obviously; and the protection of the community's privacy. The ATO has a fairly significant database of—

Senator WATSON—Did you say 'criminals employed by the ATO'?

Mr O'Connell—I said the prevention of criminals or anyone associated with any criminal activity being employed by the ATO. In terms of the checks and balances, the CPSU believes that there is a need to review those checks and balances, and they go to the heart of any concerns that may come before the committee that there are not sufficient checks and balances in the administration of the ATO at the moment. The core of that, we believe, is the reorganisation of the ATO which has occurred fairly quietly, and maybe even senators are not fully aware of the reorganisation at the top level of the organisation.

Up until 1996 the ultimate body of the ATO was the management board. Therefore, you had a fully legal body, comprising somewhere between 15 to 20 people, who oversaw the administration, so the total administration of the organisation went to that body. Whatever matter it was, the final call was with that management board. At the start of 1997 the Commissioner announced that the management board would be restructured and would be called the Corporate Business Forum, with no legal standing. The previous people who were on the management board then constituted the Corporate Business Forum—the same 15 to 20 people but without legal standing.

What then happened, in terms of the legality of the administration of the ATO the board effectively became the four commissioners, so we now have four people in charge of an organisation collecting $140 billion on behalf of the government. If you look at issues like settlements, the final call of those settlements goes within that group of four, as do other issues of administration of the organisation, and it is quite clear that those four people are operating as the board.

We have listed in our submission the names of those four people. I certainly put on the record that there is no suggestion whatsoever that any of those four people are in any way questionable. What we go to is the process of the organisation that may lead to a situation where there simply are not the checks and balances that would be required, or should be

required, by the community and the government to ensure that things untoward do not happen.

Senator WATSON—They are the second commissioners, are they?

Mr O'Connell—That is the Commissioner and the Second Commissioner, collectively referred as the commissioners. That is a serious matter for the committee to have a look at. From the staff's perspective, in terms of them doing their job and particularly what we would call tackling the top end of town, one of the significant issues has been the level of resources that have been provided to the ATO over the years. From several government sources, what has been applied is a continuing drive for efficiency. What happens with that continuing drive for efficiency is that where the ATO has to cut its functions, it does so on the things that have some degree of flexibility. The level of audit coverage gets cut because you have to process returns; you cannot necessarily cut those things. Client education gets cut—those sorts of things get cut. We then operate at very low levels of doing those things that aid the compliance of the tax system but are not necessarily things that will be achieved overnight.

In terms of the impact of that, what we have seen is about 3½ thousand people leave the organisation over the last three years, and very many experienced officers have left the ATO. That is not to say that there are not many experienced officers still there, but many have left, and it means there are a lot fewer people at the ball in terms of tackling some very difficult areas of compliance. We believe this is closely associated with a cultural process that the Commissioner has been engaged in for the last three or so years. Certainly from my direct experience, the Commissioner has employed a number of cultural consultants at fairly significant expenditure. The Commissioner can answer whether this is true or not, but my understanding is that two consultants in particular were costing in the order of $1 million a year.

It is fairly unclear to a lot of our members as to what this cultural change is about, other than to say that he wants the ATO to be a little more private sector in its methods. As to what that means, people might have their own view. In terms of that, we believe there is a danger to say to people who are experienced, well-qualified tax officers, 'What we want you to operate like is the private sector and to put away your sense of community obligation,' which most if not all tax officers do have. If they said, 'Well, we'll be in it for ourselves in terms of collecting tax and acting like the private sector, then we will claim the salaries that are appropriate to the private sector in the tax field at the moment.' We only have to look at the GST market at the moment to see what salaries are being adhered to.

Nonetheless, we believe there has been an overfocus, if not an obsession, on culture and it has not paid dividends. The end result has been that many officers were told fairly directly, 'If you don't agree with the direction or the organisation then you may as well leave it,' and many have. The end result of three years of that experience is that in recent culture print surveys by each business line, some of them are now showing that still 80 per cent of the staff disagree with the direction of the organisation, so you can see that it has not worked, if it were ever going to. There is also the side issue about how much that sort of process has cost the organisation and what it has delivered to organisation, which in our view would be very little.

I want to briefly mention the issue of service in terms of treatment of taxpayers. Perhaps not all would agree with this assessment, not even within my own organisation, but we do believe there is a new tax system being created by recent events and it is not, perhaps, one that we would support, but that is for others to comment on. What is happening within the organisation, in our view, is that whilst the GST is being introduced there is going to be an ever-decreasing focus on other areas of public administration, because I think all tax administrations recognise that a GST is going to be far more easily collectable than other areas.

We have seen in recent days what you have to go through to get some big taxpayers to pay their required amounts. We also know from a recent case that tax avoidance is certainly not dead. Whilst not wishing to comment on the particular matters at hand in relation to the Max Green case, what we certainly saw was that someone was offering a tax avoidance scheme and people were tripping over themselves to invest in that particular scheme. We certainly believe that tax compliance at the top end of town is very much a necessity and we are concerned that it might be moved away as the easy GST dollars come through the door.

In terms of service, serving the public we believe is an essential part of the ATO's function and one which we believe is being moved away from. We think compliance and service are directly related to each other, that compliance comes out of service, that compliance comes out of community presence, and we are concerned that these things are being moved away from.

In two areas, cashiers and inquiries, the ATO has made announcements with particular impacts on regional Australia of cashiers' and inquiries functions being cut down. Inquiries functions is now being run under the slogan, 'It's quicker by phone.' I guess our slogan in response to that would be, 'It's better in person,' because people do have different arrangements and they do need to talk face to face at times. In terms of cashiers and inquiries, a member recently summed it up that perhaps the ATO is an unusual body in that it is a public service that refuses to serve the public and it is a revenue authority that refuses to collect revenue. Although that is a bit quippy, it certainly summed up the feelings of many.

In terms of service, I note the ATO has established a principle around GST that 80 per cent of the tax-paying public ought to be within 100 kilometres of a tax office. We support that. We suspect that the government might have given severe guidance to the ATO in establishing that principle, but we welcome that principle. The next question we ask is: why does that not apply to all other tax matters as well, that 80 per cent of the tax-paying public ought to be within 100 kilometres of a tax office and therefore able to do their banking with the tax office and able to have an inquiry answered in presence as well as having GST inquiries answered? What about individuals? What about small business? What about partnership issues? What about what they ought to be able to have? So we support that rule but we think it needs to go further.

The final issue in the introduction is in relation to performance management. Certainly the union has been involved in the last round of agreement making and we have seen a trend of the ATO to move towards a performance management system. At one level there is individual performance based pay and that comes out of a whole set of criteria that people

are judged against. On the other hand, there is a corporate set of performance pay that is possible should certain criteria be met. Our members have raised with us serious concerns in terms of some of those criteria in relation to the establishment of performance based pay, the most notable being that audited clients get to provide feedback on an auditor's performance in the field. I guess you would only have to think about that for one second to realise that if you are going out to audit someone, they are not going to be particularly impressed if they do not like the particular outcome of that audit. Therefore we believe that that creates a situation where there would be pressure brought to bear, particularly from those who are fairly savvy I suppose, who would use that against an auditor to say, 'How about we settle for this, and then I won't complain to the ATO about your performance.' So there are certain elements of that performance management system that I think the committee perhaps needs to inquire further about.

In summary, we support the independence of the commissioner and the ATO. We believe that is important. But we believe that perhaps there needs to be a greater sense of the checks and balances within the system to ensure that those powers are controlled. We have made a particular recommendation about the term of the commissioner that we would like the committee to think about. We think the term of the commissioner of seven years is perhaps a bit long in this day and age and maybe the government is already thinking about that particular term of office, given that the current commissioner's term expires shortly.

The ATO is a community asset and we agree with the ATO in their submission on that. The way to ensure it remains so is to have what we believe is a multistakeholder review of the ATO as proposed in our submission; to interview clients, staff, managers, politicians and community groups to see what they want from the ATO to ensure it remains a good, independent and viable community asset and is administratively run with the full confidence of the community. The commissioner says it is a new tax office for a new tax system. I guess there is something we would say about ensuring that the administration is in the right mould for the future as well. Thank you, Chair.

CHAIR—Thank you. Before we proceed to questions, we received documentation from you this morning. Does that contain additional information to your original submission?

Mr O'Connell—It does in the sense that it is updated. I make just one note that the Child Support Agency, for instance, is no longer legally part of the ATO, so there are still some references that we might not have gleaned out of there. But, essentially, there is a bit of an update around various things such as the GST, for instance.

CHAIR—So we will resolve to receive the additional submission. With regard to the issue of policy development and, indeed, the staff involved, particularly in the area of recovery, have you found that there is a problem with communication exchange between the various levels? I note you do make comment with regard to senior management and staff, but have you had any cause to find that, say, between the different divisions or the business sectors of the ATO there is a lack of exchange of information?

Mr O'Connell—We do make the point in our submission that the establishment of the separate business lines, which originated in 1994—which we accepted as part of an overall agreement, I hasten to add—makes sense if you think about it in a theoretical sense—'Yes,

let's address small business by having a small business line, let's address large business by having a large business line.' It sounds good. The negative side, which we were concerned about from day one, was that this would establish chimneys within the organisation—I think in America they call them stovepipes, but the same theory is being applied there. There has been a concern that there is a lack of information, a lack of procedure, flowing between each of those bodies.

As you might be aware, previously they were functioned around debt management, they were functioned around audits, so audit procedures were audit procedures and they flowed across that group of auditors. Now you have got auditors in small business, auditors in large business and debt collection as well, so you may have concerns that those procedures are not exactly the same. The end result of that is that one taxpayer may feel, 'Hang on, this was applied to me in small business, but my individual procedure was applied in this particular way.' So I would say there are some concerns.

CHAIR—In terms of those particular units, going right through to the prosecution investigations unit, have you had any feedback from staff involved there to say, 'Well, look, there isn't a flow of information'? They are very much operating in these almost soundproofed units. Do they become little fiefdoms.

Mr O'Connell—There is always the potential that they could become fiefdoms, but I think it is a little less insidious than that. It is more the case that the flow of information does not go across because people are busy, people are under instructions to get a particular job done. But then what happens is they are operating under the management of that particular line and they answer to that line. The cross-flow of information across any of those areas—prosecutions or debt collection, whatever—does not seem to happen on a regular basis and there is no appropriate body to ensure that happens. The only place the organisation comes together is at the corporate business forum which is in national office, the very senior people of each line. That is the only place they actually come together. The cross-fertilisation at the lower level, to our knowledge, does not really exist significantly.

CHAIR—You said in the introduction of your submission at 1.7 that you have no view about allegations of organised crime:

> However, the CPSU believes this is not a significant issue. Of perhaps greater significance is activity associated with special treatment accorded to taxpayers by friends acting on behalf of agents.

Would you like to elaborate on that?

Mr O'Connell—This comes from knowledge over the years. It is not our business to jot down all the things we hear, to make summaries of those observations. We are certainly not aware of any organised crime infiltration of the ATO. The *Sunday* program is probably the first time we would have heard of that particular allegation, for a start. But over the years we do know that there have been certain instances. I think the ATO makes a reference to it in a way in their submission when they say 40 people or so have left the organisation because of concerns about the way they have been handling their job. It comes from a handful, I suppose, of circumstances where we believe people have friends on the outside, rather than any organised effort.

CHAIR—At 1.11 in terms of your introduction you say that you:

. . . do not wish to comment extensively on the high-wealth individuals or large businesses internationally, except to say that staff work extremely professionally and diligently under enormous legislative and administrative funding and even political pressure.

Would you like to elaborate on that?

Mr O'Connell—The high-wealth individuals initiative was set up because there is significant concern, or there appears to be significant concern by the government on behalf of the community about the high-wealth area. We certainly welcomed the initiative of having a high-wealth individuals task force, but what we would say is maybe there are other ways to tackle that particular issue in a more systemic way. I think that is just a comment that says the government has set this up and the government was very keen for there to be results—and we will not criticise the government for that. We are trying to seek those results. That is just a comment to say that the officers of the ATO are operating under a significant degree of pressure.

CHAIR—At section 11—which I found interesting—you say:

Several recent trends have emerged which may require deeper analysis. These include allegedly harsh treatment of less well off individual female taxpayers.

Do you have anything you can provide us with that might assist us?

Mr O'Connell—Sorry, which reference is that?

CHAIR—It is on page 14 of your original submission, section 11.1, 'Agenda and equity'.

Mr O'Connell—Once again that is a commentary of some of the examples we have seen. The *Sunday* program was, to some extent, reflective of that; the less powerful you are in the community, the less likely you are to receive favourable treatment from the ATO because it is essentially a negotiating exercise where the more power you have the more able you are to push the ATO to its limits. I guess that is a reflection of the *Sunday* program and other observations that perhaps female taxpayers do slightly worse in that particular aspect, whereas males tend to dominate the top end of town and, therefore, are more influential.

Senator WATSON—There is a difference. They might not get as favourable treatment, but are they more harshly dealt with? That is the other issue that we have to pursue.

CHAIR—Have you had any feedback from ATO staff which gave cause for this analysis?

Mr O'Connell—From our observations there seems to be that balance, in the same way there are other gender equity issues. It tends to tilt that way, rather than being something that is so overt that it stands out on a mountain.

Senator STOTT DESPOJA—It is not as a consequence of any specific ATO policies?

Mr O'Connell—No, certainly not. I do not think that is the case.

Senator WATSON—You have raised the question of collecting through settlements $60 million where a billion was at stake. Can you give some more examples of these, what might be called unbalanced settlements? Do you think the settlement process is being pushed by a need to meet revenue targets?

Mr O'Connell—It is our view that over the last six or seven years there has been a concerted effort to settle cases. We make particular reference to appeals and review, from about 1993 or so, where they had an enormous number of cases on hand. They were instructed, essentially, to try and settle. I hesitate to use the words 'at all costs', but it was not far from that. They were told to settle cases because the number of cases on hand was an embarrassment to the organisation, I suppose, but also to try and free up resources—'Don't leave these cases hanging around. Don't pursue them to the ultimate extent of the law. Try and settle them if you can.'

That flowed through. I have not got the exact figures, but we are talking of thousands of cases that were taken off the books through settlements in that exercise. There may be a question about, if you had applied the law a bit more stringently, whether you would have done that if you had had the resources to do that. You have got those really big cases that are on the record, but below that there is a concern about the procedures.

Senator WATSON—Can you give us a list?

Mr O'Connell—I am not privy to those details and it is not my job as a union official to pry into individual tax matters—and certainly not to record them. I do hear oblique references to them. But that is the impression one gains; that the matter of settlements is still very much an issue within the organisation and it really does come down to that power of who the tax office is pursuing, if that is the correct word, but also it relates to the power and the resources of the ATO in being able to do it. And it is an uneven game.

CHAIR—In terms of the feedback to the union from its membership which deals with these things, obviously there have been criticisms made that from state to state or region to region there are variations in the application. Is that something you find? Do you get feedback along that line—there is no consistency, no consistent policy approach or directional approach as to how these things should be dealt with?

Mr O'Connell—Opinion shopping has been a feature, I suppose. People have gone between offices to seek different opinions in the past. I suppose one argument in favour of the business line structure was that there was an attempt to try and do away with that opinion shopping; when people said, 'Well, I didn't get a very nice opinion from that office so I'll go to another one.' In terms of state to state, that is a big call. You would have to be a national organisation, I would imagine, for the ATO to allow you to move from one state to another in terms of the matters being addressed.

CHAIR—No, I was not asking about people doing it—the potential taxpayer.

Mr O'Connell—Sorry. I beg your pardon.

CHAIR—I was asking: from a union point of view do you get any feedback from your members involved in those areas as to the lack of guidance from management on a consistent national policy approach to dealing with those sorts of matters?

Mr O'Connell—My answer to that would be that I have not been overwhelmed by information that people are concerned. But they are concerned about direction per se. I guess one would not be critical of the ATO in trying to provide that national consistent direction within the lines.

Mr Girdler—Perhaps it is a case of not so much the policy approach varying necessarily from state to state but the concern being with the policy approach—that is, on one level the resources are not being provided to allow people to do their job sufficiently so they can take cases to the ultimate extent and prosecute them properly. We have mentioned in the submission, for example, the cut to 20 per cent to high wealth. After they have done a lot of information gathering, they are now in a situation where a lot of our members can utilise that information effectively and they are then finding cuts in their staffing. It is those sorts of pressures that are very frustrating to our members.

CHAIR—And the potential for them, in terms of their budgets, to overrun if they expend significant amounts of revenue on prosecutions.

Mr Girdler—That is right. We have also gone into some of the perceived legislative impediments as well that are really felt by our members to give business, and particularly big business, real advantages in dealing with this process.

CHAIR—It is a chance.

Mr Girdler—We have mentioned some of the sections of the tax act, for example, and the way in which they are actually used by big business and how we believe that business often uses these sections of the act to delay matters and to make them more and more costly for ATO auditors to pursue. It is those sorts of things that many of our members, particularly in the large business area, find rather frustrating because there is a concern that if the matter simply becomes too costly then it becomes more economic on behalf of the ATO to settle.

Senator WATSON—Can't you articulate those sections for the purpose of the record?

Mr Girdler—I am just trying to find where the section on agreements is listed. It is the objections and appeals provisions of the Taxation Administration Act and I am just trying to find the actual section. It is the section dealing with access to records as well, policy in relation to access to records where business is, on occasions, able to frustrate the ATO by not allowing them to readily get access to records.

Senator WATSON—But hasn't the tax commissioner been very successful using the old 264 in terms of overcoming this question of legal professional privilege? He has had a couple of successes there, hasn't he, in recent times?

Mr Girdler—That may be so. The use of 263 and 264 is an issue that is commented on at 2.6 of our submission.

Senator WATSON—Yes, I saw that. I think that might have been a bit out of date because in recent times the tax commissioner has been fairly successful there.

Mr Girdler—I do not think that would be a view that is shared by our membership.

Senator WATSON—That the court cases have not been successful?

Mr Girdler—Not that individual court cases have not been successful but overall the problems with that legislation are not still inhibitors to our members in carrying out their function successfully in the large business area.

Senator WATSON—So there is 263, 264 and appeals and objections.

Mr Girdler—Yes.

Senator WATSON—Can you tell me if there has been any reduction in the percentage of cases being referred to the AFP in favour of settlements?

Mr O'Connell—I would not be aware of those.

Senator WATSON—Where there are questions of fraud, is it ATO practice to allow settlement in those cases or just avoidance?

Mr O'Connell—Of allegations of taxpayer fraud?

Senator WATSON—Yes.

Mr O'Connell—Not to my knowledge—that wouldn't be the case. I think that puts it into a different category.

Senator WATSON—That is what I am trying to get at.

Mr O'Connell—Yes, it depends on whether you determine fraud as including criminal activity. There are certainly different—

Senator WATSON—There is a difference between avoidance and fraud, isn't there?

Mr O'Connell—There is, yes.

Senator WATSON—The act used to distinguish between the two in terms of penalty and how far back you can go.

Mr O'Connell—Yes.

Senator WATSON—In terms of fraud, have there, to your knowledge, been any cases of settlements in the event of fraud?

Mr O'Connell—Not to my knowledge. I could not tell you off the top of my head.

Senator WATSON—The use of charitable trusts have hit the headlines over recent times. Have you got any recommendations for tightening up the legislation in that area?

Mr O'Connell—No specific recommendations on charitable trusts, no.

Senator WATSON—You have not.

Mr O'Connell—We have a broad—

Senator WATSON—But you are aware that they have been used as vehicles for avoidance?

Mr O'Connell—Yes. We have a broad view about it.

Senator WATSON—Can you help the committee in tightening up that abuse?

Mr O'Connell—We have a view from our members about the use of charitable trusts, which is a fairly broad view and one which supports the view of the commissioner in relation to the use of trusts. In fact, I think we probably have a fairly significantly hard view about the use of trusts as what we would call an avoidance mechanism.

Senator WATSON—Yes, but in particular charitable trusts. Can you articulate that a bit more for the committee, as to how we should recommend there should be changes?

Mr O'Connell—I do not think it is our role, Senator, to go into details about the legislation as such. Our role, as I think I indicated at the start, was to provide a bit of a background to the framework in which the ATO was operating as one small part of the puzzle. On the issue of charitable trusts we just have a fairly strong broad view. Perhaps that is fairly hard on the spectrum that our members see trusts being used in 90 per cent or 95 per cent of cases not for the purpose for which trusts were originally enacted—that is the grandmother-grandchild type of trusts, if you like.

Senator WATSON—That comes back to the question of whether there is appropriate scrutiny by the tax office of the trust deeds before they grant tax exemption?

Mr O'Connell—Within the confines of the law we believe there are. Within the confines of the trust law we believe the review of trust deeds are adequate. We think this is a legislative question and we are quite happy with the direction that the commissioner is taking on the issue of trusts in terms of trying to tighten up the trust law.

Senator WATSON—What about loan-backs from charitable trusts and these sorts of things? They have managed to slip through a few trust deeds.

Mr O'Connell—Once again on a specific question about trust type arrangements, we are not prepared to go into that sort of detail. I appreciate your background is very much into that sort of detail but that is not our role here and now.

Senator WATSON—We are just trying to get to the nub of the problem though using your expertise and experience within the tax office.

Mr O'Connell—Our expertise is as a union, not officially as detailed tax administrators, if you like. There are not enough hours in the day to do that. But we are quite happy not to disagree with the commissioner on this particular broad question about trusts and administration. As I said, that is up to him. We do not have the time to go into the full intricacies of trust but I will reiterate that we are happy with the direction of the commissioner in trying to tighten it up. If we had our druthers we would say perhaps a much harder law across the whole trust arrangements because we do not believe that morally they are being used in the way in which it was originally intended.

Senator WATSON—The commission that you referred to are drawn from a wide sector of the public. You initially indicated that that was for the purpose of making an inquiry. Do you think the recommendation of the JCPA that they should be a board or commission oversighting or governing the tax office is an appropriate way? You were very critical of the leadership of the tax office. How are we going to improve that, apart from a commission to make certain inquiries? Would you recommend that that be an ongoing sort of board?

Mr O'Connell—It could be. This body has got some fairly serious matters to deal with under its terms of reference. What I was looking for there was a much broader group of people to oversee how the ATO ought be administered in particular in the future. That recommendation comes from experience with our United States colleagues. I hope this is relevant and interesting but the experience there was that there were some serious matters relating to the administration of the Internal Revenue Service in the United States and certainly far more dramatic than our circumstance. I am not suggesting it was anything untoward in terms of illegal activity or anything, but what happened was that their modernisation attempt fell over after the expenditure of $US1 billion and they had to look at how they were going to go through the next phase of their modernisation.

They also obviously had a very big concern about how the IRS is perceived in the community. As I said to one of my colleagues in the United States, we even make jokes about the IRS over here in terms of how they are perceived in the community. There are some different approaches there that are the cause of that. For example, IRS officers carry guns and things like that but they are very much focused about the customer end. To say, 'Let's put together a body from various groups to look at how the IRS can overcome some of those impressions and deficiencies in their administration, to gain the confidence of the American people'—to do that as a contrast here with the taxpayer charter, what we have seen is that this is a process that has been dictated to from the top. The taxpayer charter has been set up by the commissioner and his senior people to tell the community how the community ought to be serviced.

To me that is an odd way of doing things. If you want the community in many ways to feel the confidence of the organisation, you actually go out and ask the community what they want, and to do it in a fairly structured way—not just that you can send in a submission if you like—that says, 'Well, what does the community want? What do groups like ACOSS want from the ATO? Can they provide a framework for which the community feels that the ATO as a fundamental part of the community, as the revenue collector, is then providing

services through that to the community?' So it is a fairly bold move but I have seen it operate in the United States.

One of the outcomes was that, whilst the commissioner there retains his or her independence, an oversight board has been established as a legal body answerable to the president, that has a continuing role to ensure the community's objectives as established in the new legislation are being monitored. So you still have the independence but you still have a legal oversight body that says, 'Hang on, you are not meeting what the legislation says or the charter says over there.' That is where we picked up that concept and we thought it was worth having a look at.

Senator STOTT DESPOJA—In section 8 or 2.14 of the new submission you referred to privacy and you did not elaborate on some of those comments in your opening remarks. Mr O'Connell, if you would like to refer to this generally perhaps, I would be curious to hear some of the risks to privacy that you think are posed as a consequence of either funding cuts, resource cuts or outsourcing. More specifically, I would like to refer to 2.14.6 in relation to the organisation processing employment declarations. I was hoping you would make clear to the committee the information that the CPSU has in relation to that. Bearing in mind you are under parliamentary privilege, I hope you will take advantage of that to put on record any information you have in relation to what seems to be a blatant breach of privacy protection.

Mr O'Connell—I will start on that issue of privacy by saying we have had our own little example of that recently, and you may have read in the media about it. It was indicative of what could go wrong, if you like, and we certainly have a fundamental view that if you outsource you lose control of process because, at least as a minimum, you then have one extra step in terms of the distance between yourself and another organisation.

What happened recently was the ATO outsourced the production of its own group certificates. The tax office actually outsourced production of group certificates for its own employees which, to me is, at the least, a little bit ironic. What it created was distance between itself and the other organisation and, as a consequence, there were some serious muck-ups in the production of those group certificates or, more importantly, the delivery of those group certificates.

We had cases where other staff members received other people's group certificates. We had lost group certificates for 1,000 out of 15,000 employees. That is one in 15. Extrapolate that to the general population, if you like, in terms of privacy concerns. People had their group certificates sent to their home address with their work location still written on the envelope so their next-door neighbour or someone could have seen that envelope and found out where they worked. Particularly in relation to the Child Support Agency people are very concerned about their privacy at work. The organisation they outsourced it to, I suppose, is also the organisation where the employment declarations are being sent to.

Mr Girdler—That organisation also distributes material on behalf of the Child Support Agency.

Senator STOTT DESPOJA—What is that organisation?

Mr O'Connell—It is an organisation called Salmat. You may be aware that there have been some other concerns raised in the media about that particular company, in South Australia and Western Australia particularly, I think. So that is the organisation where you are talking about having employment declaration forms produced. You are talking about a range of other material produced and we have become aware that that organisation has, as another major feature of its activity, direct marketing work. I cannot say that we have any evidence to suggest that tax data has been used in that direct marketing work but it is only one step away from there, in this day and age, where the appropriate IT technology could transfer some of those, either with or without the knowledge of the organisation, through a bad apple in that organisation, to an inappropriate mechanism.

I think we are all concerned about the level of information going around about ourselves from whatever source. It is very hard to say, 'What source does it come from?' As an individual I continually receive phone calls from people trying to sell me things, obviously based on some database issued by someone I do not know and ending up in some call centre somewhere. I am sure I am very much not alone in that aspect. If you had a track of the ATO through a private sector organisation with the database and then out to some private sector organisation which wants to buy that database, either legally or illegally, then you might not even be able to track it back. Maybe in another place there is a look at that legislation about privacy in relation to the selling of information.

The bottom line, in terms of all those sorts of things being outsourced, is that the ATO has one of the most comprehensive sets of data on the Australian population. It has your name, your address, your income, your occupation, your spouse's name, your shares, what you own, et cetera—a whole range of things. Of course the more complex your tax affairs are, the more information in that database. Our overall view is that database ought to be sacrosanct. It ought to be sacrosanct, both for the Australian population and also for our own members.

Senator STOTT DESPOJA—How do you ensure that it is sacrosanct? Obviously we have legislation that relates to the public sector; we have privacy legislation. Obviously privacy legislation to extend to the private sector is coming very soon. Are you advocating or recommending tighter criteria or legislative changes both for the public and private sector legislation? Are you also suggesting that perhaps your members are aware of other privacy breaches that may not necessarily relate to outsourcing of the use of technology? Is this something of particular concern to your members?

Mr O'Connell—I think our members have a very heightened sense of privacy. It has been drummed into them quite appropriately from day one that the privacy of taxpayer data is sacrosanct. When they see their own privacy breached they certainly jump up and down fairly quickly and strongly. In terms of the legislation, I could not say that we would make specific recommendations on it. The one recommendation we would make would be the simple one—that is, that the tax office must look after its own data and should not outsource it, because you cannot guarantee that it will not get out in some way, shape or form. I think that is the fundamental principle, that this data is sacrosanct.

IT outsourcing is, of course, the big one and maybe there needs to be a review of that decision to outsource. Our members certainly have an extreme concern that outsourcing to

EDS may lead to breaches of privacy in the future. That is aside from the other issues where they also believe it is going to cost the government more. But on the privacy front we cannot guarantee—even for an organisation that is perhaps as well known and as big as EDS and perhaps in some circles well regarded—that there will not be a loss of the privacy controls because you are no longer in control of that data. There are many people who work in EDS and you really only need one bad egg in there to perhaps duplicate some of the records and then off they go and you never know what happened to them or where they went.

Senator STOTT DESPOJA—You obviously see a role for the privacy commissioner on the commission of stakeholders that you advocate.

Mr O'Connell—Yes, we certainly do. That is one of the stakeholders we see as very important. As I understand it the Australian Bureau of Statistics made a decision I think not to outsource any of its data. There might be a debate about which is the more sensitive area of data—the census material or the taxpayer records. Some might say the census has got more in it, some might say the taxpayer data has. Nonetheless, they would probably make the same judgment, that we believe there is too much data in there about too many Australians for you to give even that one per cent risk of outsourcing it.

Senator STOTT DESPOJA—Can you just briefly put on record the instances in WA and SA to which you referred, just for the benefit of the committee, and at my colleagues' urging.

Mr O'Connell—I actually have not followed up more than the detail in the press. I was just going to let the processes that were under way there take their course. I think allegations within the state governments there are that some of the data had been breached by Salmat.

Senator STOTT DESPOJA—In relation to gender and equity you have answered my colleagues' questions but you do recommend that the issues in relation to the treatment of less well off individual female taxpayers should be examined in more detail. How? Through what processes would you recommend that takes place?

Mr O'Connell—We have raised it as a concern and maybe there is nothing in it ultimately. One would hope that that is the case, anyway. We are not saying that there are direct discrimination policies in relation to our own membership but what we have seen is a systemic outcome—in relation to redundancies in particular—where the number of women and the number of people from non-English-speaking backgrounds has been disproportionate. I could point to offices in Victoria where the number of people who have walked out the door with redundancies from perhaps the Indian and Sri Lankan communities seems to be significantly disproportionate and that perhaps needs to come onto the record.

In the same way, I think it is just perhaps reflective of the community that the people with power tend to be, as a percentage, male and the people without power, as a percentage, tend to be female. From our evidence what the ATO is doing—and I am not blaming the ATO necessarily for this because I think it is part of the overall resource balance that the ATO has to cut its cloth at times according to what it can do, and that tends to be that we cannot fight certain powerful individuals, such as Kerry Packer, to the fullest extent. Mr

Packer has signed up every tax QC in Sydney to defend his case and it is very hard to compete with that. But at the lower end of the scale, you can just imagine the situation: you are a single mother and you have a tax issue with the tax office, how on earth are you going to take them on? The tax office would make the judgment, 'No, the law applies. Sorry, the law applies in that case.' There is not much you can do about it as an individual.

Senator STOTT DESPOJA—In relation to settlements is there an argument for greater transparency? I know you have answered this partly in relation to Senator Watson's questioning but do you have a view as to the guidelines surrounding settlements and whether they should be public? Obviously you refer to a couple of extraordinary settlements in your submission.

Mr O'Connell—I am just trying to recall the commissioner's position on this. I think his position was that there ought to be a public record of those. Certainly that is what is now being proposed in the United States, the issue of settlements being put in some way on the public record. I could not tell you exactly how that is going to occur. I would support a public recognition of settlements. I think there is also a suggestion by the commissioner that there be—I forget the exact term—a good taxpayer's recognition as well, from good corporate citizens. I think perhaps that has been lost a little bit—the good corporate citizen approach. Maybe that is reflected on the positive side as well. We would suggest it is a good idea to have those public records of settlements. If the parliament or elements of the parliament then say, 'Hang on, why has the ATO reduced a billion dollars down to $60 million in this case on four occasions over the last couple of years, costing potentially the revenue $3½ billion or more?' there must be something that says, 'Hang on, why is this so?'

On the other hand, and I think this is a also a good thing, what it does is make sure the ATO, at the first call, is very stringent about raising the assessment so there is no leeway created. I have nothing to suggest that this is the case but if you know that you are going to head down a track of having to settle at one particular point in time, then you actually raise the debt as a negotiating position. You could do that. It is like going in with an ambit claim for wages—not that we ever do that, of course—but there is a suggestion that keeps the whole system more honest, I think, from both ends of the spectrum.

Senator WATSON—Mr O'Connell, when settlements are made, say in Victoria or New South Wales, does that have to be referred to a central office, say this committee of four that you were referring to? What is the process there? Can it be made at a local level, for example?

Mr O'Connell—It depends how big they are, I guess.

Senator WATSON—What are the rules?

Mr O'Connell—It is certainly the practice that large settlements go to the national office of the ATO and normally to the head of the relevant business line.

Senator WATSON—Is it a graduated scale, settlements under $100,000?

Mr Guthrey—In relation to settlements and matters like that, Senator Watson, there are certain limits and authorisations within the ATO. Generally it depends on the size and the taxpayer involved in relation to that. I do not have the figures in front of me but, for example, generally settlements involving tax payable up to say, $10,000, would be allowable by reference to just a manager or a team leader within the organisation, then you go up to various levels of SES, and very large ones would have to go to the commissioner.

CHAIR—So there are set policy guidelines, in fact?

Mr Guthrey—Yes, there are authorisations.

CHAIR—I thank the CPSU representatives for their submission and the evidence given to us today.

Mr Guthrey—Thank you, Senator.

[11.33 a.m.]

STOLAREK, Mr Anthony, Partner, National Tax Competence, Arthur Andersen

WACHTEL, Mr Michael Howard, Tax Practice Director, Arthur Andersen

CHAIR—I now welcome the representatives of Arthur Andersen. The committee prefers all evidence to be given in public but under the Senate's resolution you have the right to request and to be heard in private session. Before we proceed, may I also draw to your attention the nature of this and other Senate committee inquiries. Senate committees do not have the power to make determinations or orders and do not function as a dispute resolution body. Without pre-empting the committee I would point out that, based on past practices, it is unlikely that the committee will make recommendations on individual cases. Rather, it is expected that the committee will explore a number of individual cases in order to draw conclusions on general or systemic issues in the operation of the ATO.

Because of this, the committee wishes to avoid receiving evidence that constitutes adverse comment about individuals as far as possible. If you wish to refer to an individual adversely, you should be aware the committee is obliged to extend a right of reply so you should, wherever possible, refer to them as Mr or Ms X, et cetera, rather than by name. If you do wish to refer to an individual by name, we request that you advise us first so that we can consider whether we should proceed in private session. I now invite you to make an opening statement.

Mr Wachtel—We would suggest our submission does speak for itself. Our submission and our time here this morning is part of our attempt to play a constructive role in the context of your committee. Tony Stolarek will make some opening remarks and we are thereafter very happy to answer any questions.

Mr Stolarek—The view of our firm in relation to the particular matters that the committee is looking to is that much of the concern about the tax office to our mind can be explained by reference to the tax law. Taxation is quite complex, given the complexity of business, and the business environment is becoming ever more complex and internationalised. We see, therefore, one of the key roles of the tax office and, indeed, the government, is to ensure that the law is continually updated and kept relevant and appropriate.

We have a lot of regard for the effort of the tax office in modernising the tax office and changing its orientation. Our key observations would be that the efforts of the tax office should more profitably be devoted to improving the law and ensuring that the understanding of the improved law is consistently communicated to all taxpayers. Our initial observation is that if we, in fact, have bad tax law or obsolete tax law that has not been improved for many years, of necessity that creates loopholes or arbitrages and opportunities and those opportunities are available to every taxpayer who is well advised enough to find them.

We recommend a stronger resourcing of the tax office's technical function and legislative and policy development function. A key focus ought to be an improvement of the law. That will, in fact, make a lot of the concerns about equity disappear, which to our thinking are

somewhat misconceived. We recognise the efforts of the tax office in this area and, as I say, our key focus is that by a process orientation within the tax office on law improvement and disseminating technical knowledge into the community, one can in fact achieve a more equitable and balanced outcome for all taxpayers. Thank you.

CHAIR—Thank you, Mr Stolarek and Mr Wachtel. In regard to the consistency issue, at page 4.4 you say, 'The ATO is addressing but has not succeeded in ensuring internal consistency of tax opinions across Australia.' You further say, 'This can cause differential interpretation in different offices of the ATO.' Could you add further to that and give us some examples, if that is possible.

Mr Stolarek—The systems issue can be explained as follows: until the tax office elaborates on a technical position which is available nationally through its internal database or through public rulings, then it becomes the role of every individual tax officer to interpret the law in respect of particular cases. We believe, Senator Murphy, it is in fact inevitable that until matters reach the tax office's private database—which we are not aware of—or the public rulings process, then it is inevitable that individual officers will be making decisions. We recognise the efforts of the tax office to improve its database—we understand a lot of effort has gone into that—but some forum shopping will always be the case.

The consistency may be coloured by attitudes of individual officers. If some officers have a jaundiced view of taxpayers they might tend one way in their decision making process versus another way. So inconsistency is always evident in preliminary fact situations unless and until the tax office has all its decisions available to all of its officers in its database. It is the same when professional advisers give inconsistent advice because there are legitimate differences of view. From a process point of view, given your desire to ensure equitable treatment, a key issue which many advisory firms, including ourselves, pursue is to try to ensure that decisions and advices are communicated. There is a strong focus on training to ensure everyone is operating in a like manner across the country.

CHAIR—I would measure the question I just asked you against a statement further on in your submission where you say, 'There will always be gaps in the law which will work against the interests of the ATO,' and also, I suppose, the circumstances that the ATO might find itself in, in that it is often required to negotiate outcomes. Doesn't that create inconsistencies of its own nature, and would you want that removed?

Mr Wachtel—The challenge of sharing information which Tony mentioned in the context of the tax office is identical to the challenge that most businesses are going through. It is not just a tax issue. It is not just an ATO issue. We are living in a totally new age in terms of information and access to electronic information, databases and so on. If you take that as a backdrop to Tony's comments—that is, we are discussing the operation of the tax office in the context of the new economy—it is more of an information age challenge than there being gaps in the law. Gaps in the law arise because economic activity will, generally speaking, always be in advance of legislative reaction to that activity. So I see them as two very separate things, Senator.

CHAIR—But is it not the case that if you have everything black and white that says, 'You are required to pay tax for these reasons' and, 'You are allowed to make claims for

these reasons,' that businesses usually employ tax accountants, et cetera, for the purposes of trying to get an outcome and look for the gaps in the law to maximise the benefit to the company or to the individual?

Mr Wachtel—What I think Tony was emphasising was that the consistency of approach issue is a challenge in the context of leveraging information throughout the tax office, to all the different tentacles, to ensure the application of the law is consistent.

CHAIR—But how do you get that?

Mr Wachtel—In our organisation we are treating that as a specific challenge in the context of operating the new economy. We are spending more money, applying more resources, employing more people whose sole function is the sharing of information through technology to ensure a consistent base. Senator, I am going to come back to your point about gaps. I was not looking to avoid that question. I am just trying to emphasise that Tony's remark in this context was more to do with ensuring that there is no potential inequity through a particular taxpayer in Western Australia being treated differently on the same technical issue as a particular taxpayer in Sydney, because in Sydney two tax officers might have the same access to a particular settlement which the person in Western Australia—who is handling a similar case with same fact pattern, same law—does not have the same access to.

Senator WATSON—That is easy to say, but can you back that up by practical examples?

CHAIR—That is what I was asking for, some examples of that occurring. This is an issue we have to take up with the tax office and in doing so we at least ought to be able to say, 'Look, Arthur Andersen have told us these things,' but we probably need to be able to substantiate that to some degree. Without necessarily naming the taxpayer, can you refer us to the particular issues of law where different interpretations or different decisions were handed down by the tax office? You can either give that to us now, or you can take it on notice.

Mr Stolarek—To put my comments into context, Senator Murphy, the issue of differences in tax office decisions really arises across the entire spectrum of taxpayers. It arises from differences of opinion as to whether particular expenses might be deductible in a salary and wage return all the way up to major businesses.

CHAIR—It is probably a little bit more clear, though, in the salary and wage returns than it is when you move into the business sector.

Mr Wachtel—I think less scope for inconsistency.

Mr Stolarek—Yes, potentially, but some of the recent areas that have been concerning the business community have included, for example, leasing; as to whether a particular transaction should be categorised as a lease or a purchase. That is an issue which, in fact, is currently receiving attention in the Ralph review. In fact, the Ralph documentation, the

platform, is almost an inventory of the issues that have been uncertain and have been causing decisions on both sides of the equation to emerge over the last few years.

There is the issue of deductibility of expenditure in a business environment where, for example, a taxpayer is involved in property development and in some cases might have received a tax deduction for interest expenses, whereas another taxpayer—the famous, recent case of Steele in Western Australia—was denied a tax deduction and the matter was pursued all the way to the High Court and the taxpayer received her income tax deduction for interest in the construction phase of a motel development. That actually illustrated the point that there were divergences of view. The deductibility of interest in a property development, a motel—this was not a multibillion dollar business, but a motel—was not a matter that had received attention and had been promulgated into the community.

To give you another example, Senator Murphy, involving the use of bills of exchange facilities, if someone borrows from a bank today they will typically be offered a choice of a housing loan or a bill facility. It may surprise you to know that the precise tax law dealing with deductibility of interests or costs under a bill facility to this day is not known. It is possible for divergences of view to arise.

Regarding foreign exchange gains and losses, there was a case of ERA, two years ago, which caused significant questions about the way foreign exchange gains and losses in this country should be treated. The tax office—and we respect the decision of the tax office here—decided to pursue a business as usual approach in relation to foreign exchange gains and losses which suited the needs of many taxpayers, Senator.

What it meant, though, was the practice diverged from not only the black-letter law, or lack thereof, but even from court decisions. So what you end up with is a practice on the part of the tax office—and again, we understand the pressures the tax office is coming from—where there is a desire on the part of the tax office to maintain a functioning system while the law does not fit the current day realities of that system and its complexities. That system often operates equitably and in the interests of taxpayers. In fact, we applaud the tax office decision on ERA because at least it kept the creaky system operating.

The problem is, Senator—and this was the main focus of our submission—that really we would expect the tax office and the government to have a strong focus when defects are exposed like that to in fact improve the law immediately, transparently and equitably for all taxpayers.

CHAIR—Just going back to the issue of Western Australia and I think New South Wales, if I understood you correctly, you said there was a decision on the same technical aspect of tax—

Mr Wachtel—Senator, that was a hypothetical example of a tax officer conducting an audit and not having the same access to the appropriate level of decision making on that issue in the tax office and the possibility that, because the law is complex, the two tax officers in different states could have a different view on the same technical issue.

CHAIR—I understand that from a hypothetical point of view. What I am trying to get to is for us to say to the tax office, when we have them before this committee, 'Look, it's been put to us that there are inconsistent approaches by tax officers'—which is what you are saying in your submission—'that leads to inequitable treatment of taxpayers.' When I was asking you for an example, you gave me an example where you know the tax law and the application of it as regards a claim where two officers in New South Wales have handed down a decision to a taxpayer with one application; in Western Australia there was another taxpayer, same technical aspect, et cetera, who received a different decision from a tax officer that ended up in the High Court. The High Court ultimately delivered the outcome about the two officers in New South Wales. With regard to that, is that now hypothetical? It is not a real case reference?

Mr Wachtel—If I gave you a real case reference—and I cannot obviously use the area of law because that would be inappropriate from a privacy point of view going back to the earlier discussion—I am aware of a case where—

CHAIR—It may be that we actually have to take that evidence in camera because we cannot, I do not think, proceed to put to the tax office or the tax commissioner hypothetical cases. He will say, 'We are not in a position to respond to hypothetical cases.'

Mr Wachtel—I will put this then to the committee and to the government: I do not think that they need specific examples to appreciate that the pace of change is such that the need to invest additional resources into the area of ensuring interpretations of law and information sharing are improved, because that challenge is the same as the challenge we are all going through in the private sector.

CHAIR—I do not necessarily dispute that point, but for us as a committee with the terms of reference we have, in looking at equitable treatment of taxpayers we have to be able to say—and there is a view that you have put to us both verbally and in your submission that there is inequitable treatment of taxpayers because there are different interpretations being placed on various aspects of the tax act—we cannot proceed then to question the tax office and put an argument to them based on hypothetical cases.

We, in fact, have to have some reference to real cases where we can say, 'Look, there was a decision based here which was different here and this ended up there and the outcome was the same.' We can question the tax office. My view would be, if your hypothetical case was in fact a real case, for me to say to the tax office, 'If the New South Wales branch made this decision and the Western Australian branch made that decision that ended up in the High Court but the final decision was X, what's happening here? Why is there this inconsistency?'—which you raise.

Mr Stolarek—Yes, we understand your point, Senator. We might take that on notice.

Mr Wachtel—What we will do, again to try and be constructive, is go back and think if we have some generic examples that we can use.

CHAIR—That would be useful when we get to deal with the tax office.

Mr Stolarek—Certainly.

Mr Wachtel—I would not like to lose the emphasis of my earlier point that this challenge is irrespective of the new economy and the age we are living in.

CHAIR—Yes, they are separate in part as well.

Mr Stolarek—Yes, I would also like to make a comment, again picking up Michael's point and the point I made earlier, that our suggestion is that, given the complexity of business and taxpayers' circumstances in this country, we would expect that not every decision by every human being in the tax office is going to be identical. As no doubt you find in other areas of the government's interface with the community and indeed in business, individual people will always have their own shades and colours of decision making. We will consider, though, whether we can put to you some fact situations, Senator.

CHAIR—Thank you.

Senator WATSON—What codes of conduct does your firm insist upon when officers are recruited from the tax office to work on behalf of particular clients who then interface with some of their previous colleagues in the tax office?

Mr Wachtel—Do you mean would we allow an ex tax office employee to work on a client where the client might be in a dispute with the tax office and the issue at hand is an issue which this employee was involved in?

Senator WATSON—Not necessarily involved in but has the potential to establish networks because of his former association. Do you have a code of conduct?

Mr Wachtel—We do not have a written code of conduct on that issue but we do have very high respect and ensure that we respect the rules which apply to ex tax office employees in terms of the obligations on them when they leave the tax office. What we have found is that some of the ex tax office employees who have specialised knowledge in certain of the more complex areas of a tax law do end up working in our firm in those areas of tax law.

We are more concerned about ensuring you do not use information you had from the tax office re a particular taxpayer, et cetera, and that you would not work on a matter where you were involved on the other side in the past. But we do not impose restrictions about what we regard as generic technical know-how in regard to those particular practice areas. We therefore would not preclude an ex tax office person who worked, let us say, as a mining specialist. We would expect that person, once they had joined us, to work in advising clients in the mining industry. We would control that issue in terms of conflicts more by reference to what the person worked on in that context.

Senator WATSON—On the other hand, in the case of a mining dispute with the tax office, say involving a settlement—it has been put to the committee and it is in some literature—that these people are in a position to establish—and have established networks because of their connections with the tax office—a special advantage in terms of securing a

favourable settlement, even perhaps something not proceeding to prosecution. That is a bit of a worry.

Mr Wachtel—In my experience I have not come across that. What I have seen is those particular tax office people with those networks able to access those networks to discuss technical issues. Also, when it comes to disputing technical issues, they can enter into debate on the meaning and interpretation of those issues. I have never come across, in our firm, a situation where I have seen an ex tax office person get any favourable treatment in the context you refer.

CHAIR—How would you know?

Mr Wachtel—Let me say, first of all, that my comments on that question are based on my personal experience. If a partner elsewhere in the country used an ex tax office person in that way, I believe it would get to me through our communication process and we would not countenance that type of behaviour. I am drawing a very strong distinction between using expertise and being involved in negotiations and literally fighting very live issues for our clients as opposed to obtaining favours. My emphasis was on the 'obtaining of favours' aspect.

I would not be surprised if there were cases where, through personal relationships—and I am not discussing my firm nor any other firm—I could see how a particular matter could be fast tracked in certain respects, because the amount of time to get to the nub of the issue which causes the problem could be accelerated somewhat because the ex tax office person and the tax office person know exactly where the tension lies. To amplify: if there were a major transaction which took six months to get a ruling on, if the ex tax office person and the tax office guy know the particular issue relates to the interpretation of a particular leasing provision, or an expense quarantining provision, or a control foreign corporation provision, you can go straight to the issue and almost determine whether this thing can go ahead or not.

Senator WATSON—I appreciate your firm's standards in this area but are you aware of these allegations that this sort of behaviour does take place in terms of getting favourable settlements?

Mr Wachtel—I am not.

Senator WATSON—I am saying outside your firm are you aware of these sorts of things?

Mr Wachtel—No, I am saying I am not.

Senator WATSON—You are not aware of them?

Mr Wachtel—I am not but that does not mean that it does not exist. I would have thought that if a firm was obtaining any favourable treatment in that context—

Senator WATSON—Not the firm, the client.

Mr Wachtel—No, but then the firm does. What the firm is saying is, 'We could obtain favourable treatment through hiring this ex tax office person.' If that were the case, it would not surprise me that I do not know about it. I would have thought that would not be something which people would be prepared to say. Tony, if you think I am looking at it through tinted glasses, please tell me.

Mr Stolarek—No, I would confirm that. I am not sure, Senator Watson, what level of tax we are talking about, whether we are talking about a deal being in our area or small business, et cetera.

Senator WATSON—No, the large area. I think the integrity, from what we have been told, from small areas is reasonably good.

Mr Stolarek—We are certainly not aware of that. Our focus is principally large businesses and so on, including large private groups. Our experiences have been always of vigorous debate. We are certainly not aware of the practices that you are referring to.

Senator WATSON—I am not criticising vigorous debate or discussion of technical issues but the interfacing in terms of settlements.

Mr Stolarek—No, we understand that. But we have no awareness of those.

Senator WATSON—There seems to be some currency about that.

Mr Stolarek—From the viewpoint of process, part of this may be, as Michael outlined, just people's general awareness of the limitations and guidelines. It comes back, again, to the higher the degree of transparency and so on, the less the value that comes out of the knowledge of internal tax office guidelines.

Senator WATSON—How do we improve that transparency in terms of the settlement area? If we are told there was one settlement for $60 million in respect of a dispute of a billion dollars, we are talking about something pretty large. How do we improve that sort of transparency and, at the same time, keep within certain privacy guidelines?

Mr Wachtel—We have discussed this particular issue amongst ourselves. It would be quite easy and quite glib to say that we are in favour of transparency, but we have come to a final conclusion that it is not that simple to merely say all settlements should be transparent. We have found in our experience that at times we have been able to obtain settlements by showing the particular fact pattern was sufficiently different from what appeared to be the fact pattern that a different settlement was appropriate to another taxpayer or preordained tax office position.

While we can see the merit of increasing transparency in certain areas, we are concerned about whether a total transparency does give you the right answer. We have not come down with a view that it should not be, but the reason why I chose to take this question rather than Tony is that we have been debating it and we have not yet come to a view that we would say transparency is the definitive answer.

Mr Stolarek—An example, Senator Watson, of Michael's point is that in the US there is, in some areas, a greater level of disclosure—for example, in transfer pricing—but that comes, of course, out of the US environment where public entities and so on have a much higher level of general disclosure of their affairs in the community. So in that area, to take one example, there is a greater array of publicly available material that has emerged from the IRS than would happen in Australia, but that again is consistent with their general community and business environment as Michael has outlined.

Mr Wachtel—The other thing is that the US do not have a catch-all anti-avoidance provision like part IVA. Part IVA is always dependent on its facts and it is sometimes easier for a jurisdiction like the US to be more forthcoming in certain areas because there is not this catch-all anti-avoidance provision. So I do think there is a distinction between us and the US in this context.

Senator WATSON—Are you in favour of the suggested tightening up of the overall catch provisions as part of the Ralph recommendations?

Mr Wachtel—At this stage we could not really answer that question until we see what it means. Part IVA is a very widely drawn anti-avoidance provision already. The fact that in the last week or so there have been some major tax cases involving part IVA is evidence of that. I would suggest that as a firm we will wait to see what those comments mean from a more technical and legal point of view before we take a view. The reason why we are concerned about merely once again answering glibly and saying, 'Yes, we are in favour,' goes back to this question of complexity and fiscal certainty.

Our main concern is that in a very complex business environment if the anti-avoidance provisions are drawn too widely you end up with low fiscal uncertainty—that certain transactions clearly would not run foul of the tax act; the degree of nervousness about running foul of the anti-avoidance provision just becomes too pronounced.

Senator WATSON—But what you have now is increased complexity of the tax law because most sections now you have attached to it an anti-avoidance provision. It is almost a double jeopardy.

Mr Wachtel—Yes, but I would put to you that if one took an example like capital losses, a specific anti-avoidance provision which backs up the grouping and capital loss provisions and which is tailored to what the government are aiming for—influencing behaviour, so to speak—is more effective than a very wide catch-all which might render certain transactions which are not offensive—those transactions would not occur. There is a very strong body of opinion, Senator, that while our tax act is a patchwork tax act and there are problems with it—and we concede that—there are concerns about having too wide an anti-avoidance provision and doing away with all the specifics because the effect could be to increase fiscal uncertainty and also not be sufficiently honed in on where the abuses are. But at this stage we applaud some of the initiatives taken by the Ralph committee thus far. The devil will be in the detail, but pending the release of the Ralph report we would expect that an appropriate balance will ensue.

Senator WATSON—In your earlier comments you mentioned the need to rewrite some obsolete tax law. Can you identify those areas?

Mr Stolarek—Some of those areas are currently receiving attention. To take some current live examples, the rules dealing with infrastructure and contracting out and transactions involving government have been the subject of rules, section 51AD division 16D, which do not sit well with current commercial practices. Those rules arose out of transactions involving state governments and, given the current trend of outsourcing, the rules do not interface properly with the commercial arrangements. The legislation has been known to be deficient for about three to five years or so. We understand it is finally to receive attention in the Ralph review and the business tax reform process. That is one example.

We touched earlier on the fact of the tax treatment of bills of exchange. Charges by a banker under a bill facility as of now are not the subject of any legislative guideline, Senator. As we know, the use of bill facilities has been in common in Australia for 20 to 30 years. Again those issues have been identified.

Senator WATSON—It is the purpose for which the funds are used, not the instrument that is used to finance the transaction that is important, isn't it?

Mr Stolarek—We expect that, yes. You are right.

Senator WATSON—Then why are you doubting that principle?

Mr Stolarek—Senator, you will recall the decision of the Coles Myer Finance case which was heard four years ago or thereabouts, I think. It was not until that decision that the precise timing of the tax deduction for bills of exchange in one particular fact situation was sorted out. That case did not relate to every bill facility in every scenario, but it related to some of the more common facilities. That case, which took a large number of years to come before the court, was needed to have the matter resolved. We referred earlier to the ERA case in relation to foreign exchange gains and losses. These are business type tax deductions but they illustrate the uncertainty and the possibility for different positions to be taken by taxpayers.

Senator WATSON—But that uncertainty will always be accentuated when business is at the cutting edge and, at the same time, creating new types of products that did not exist before—hybrids and all those sorts of things.

Mr Stolarek—Yes.

Senator WATSON—How do you suggest that the tax office can keep up with the propensity of business as business develops these new hybrid types of products which are aimed to get around particular aspects of existing law?

Mr Wachtel—One opportunity would be to have, I suppose, a more flexible technical corrections regime such as in the US where, as information comes to bear in terms of these types of instruments, if the government determine that they do want to deconstruct the effect

of the hybrid, then the response is found in the legislation. But let me say that I think we should be cautious. Sometimes these very instruments create advantages for Australia because the use of a particular instrument which is new, innovative and might have a tax result that is advantageous, has the effect of reducing the cost of funds for a particular project in Australia. So in my view the fact that the particular instrument is new, innovative and is not specifically governed by the tax act does not necessarily mean that is not good for us as a country.

It is the same as going back to 1984. The Treasurer at the time, Paul Keating, wanted to attack the use of certain types of doubled up leasing arrangements, as well as the use of dual resident companies. I think when it was pointed out that outlawing the use of certain doubled up leasing arrangements was not in the interest of Australia as a country, those provisions did not ever eventuate. It was discovered it was in our interests to reduce the cost of funds for Australian borrowers in many situations. I think there is a certain level of emotion in the tax office when they come across terms like 'hybrid instrument'. I think at times their approach to challenging those instruments is not always based on my view of what the law says, it is based on their attitude towards the use of those innovative types of arrangements.

Senator WATSON—How do we establish structures? Firstly, you appear to agree with the technical corrections bills to come out at various times but behind that there has to be a structure to pick up these sorts of new innovations and to keep the laws up to date.

Mr Wachtel—I thought that efforts had been made in this area and the tax office was quite proud of how much more quickly they have compressed the time frame between new products being in the marketplace and their awareness of those products. In some cases, as I understand it, not so much in the big corporate area but more in the private client area, they have come out with announcements almost on a current basis, where they have attacked the use of those types of arrangements.

Senator WATSON—Is there any private input from the Institute of Taxation or other professional bodies into that particular section of the tax office, or their pronouncements evaluated it in any way?

Mr Wachtel—The Tax Institute would be more involved in responding to what comes out of that unit than being the provider of information to that unit.

Senator WATSON—How do you interface as a profession with that unit to ensure that it is not going to be a decision that is not in Australia's national interest or something? Who has the job of reconciling our national interest vis-a-vis increasing the revenue? Who is going to be the arbiter?

Mr Wachtel—I think the current law is the arbiter. If there is a need for change that is an issue for government.

Mr Stolarek—We did make a recommendation, Senator, that we believed the tax office, apart from the technical corrections focus, would be advantaged by having a board or an oversight group which would not only have the role of providing a communications link but would also champion worthwhile initiatives by the tax office such as, for example, a better

legislative corrections regime. This is not an issue of any one government or another; it has been a problem over the last many years. Because of government resourcing typically the only tax changes that are made are matters where the tax law is perceived to be totally unsatisfactory. There is not an ongoing repairs and maintenance activity.

A board could be useful and to answer your earlier point about the interface, as Michael has outlined, the Strategic Intelligence Unit I do not think was dealing with professional bodies when it was originally created. The tax office has been—and again, we recognise this—creating several forums across various specialist areas. Some of these have come into being in the last 18 months or so. We would imagine that the tax office is using the intelligence it is getting from the two-way traffic in its design of performance improvement.

Senator WATSON—Is there enough transparency?

Mr Stolarek—The official minutes of the various committees, like the Australian Tax Practitioners Forum and the Tax Liaison Group, et cetera, are published. There is not any visibility in terms of where the matters are necessarily going within the tax office. Once the issues are identified, what tends to happen—and again we refer to this in our submission—is that a cloak will descend. That is to say, the decision making process is within the tax office and typically the community will see only the final legislation or a draft ruling after quite a lot of thinking has taken place. There is not an open debate across the benefits or otherwise of particular areas. This is again one of the issues we identified. What tends to happen as a result, Senators, is that the legislation itself is slowed up and the process becomes disputatious.

Senator SHERRY—I notice on page 7 of your submission at point 11 you say:

> We suggest the ATO is sometimes too oriented towards fact finding when responding to rulings. As a result it is difficult to get rulings in a reasonable time frame.

But surely the ATO has to gather as many facts as is possible in order to establish a ruling, and hopefully a ruling that will not then be challenged.

Mr Stolarek—Yes, we agree with your point, Senator Sherry. One possible solution is a package of rulings that is based on assumptions that are clearly enunciated. We have noticed the tax office using it a little bit more in recent times. That gives the taxpayer a clearer picture of the intent or the orientation of the tax office. What has tended to happen in some scenarios is that there has been a large assembly of facts in order to assemble the decision. Really what the taxpayer has been looking to is the guidelines or the concepts or the principles that underlie the decision process. We have noticed, with approval, an increased use by the tax office of a set of assumptions that is outlined and a clearer statement of principles, rather than just a conclusion.

Senator SHERRY—Would you, as a firm, ever advise a client not to make disclosure of all the facts? In what circumstances would you do that?

Mr Wachtel—We would never go for a ruling and not disclose all the relevant facts. Even if you left out certain facts which obviously were factual, by leaving them out you destroy the efficacy of the ruling. The ruling is only as good as the facts you provide.

Senator SHERRY—Yes, I understand that. But surely there must be instances where not all the facts are provided.

Mr Wachtel—We would never advise a client to go for a ruling and not disclose all the relevant facts. If there were facts that were going to hurt your case which might result in you not being able to obtain a fair ruling, you might not go for a ruling. I cannot talk for other firms but Arthur Andersen would vigorously convince the client that if they want to obtain a ruling they must be prepared to provide all the relevant facts; otherwise the ruling is not worth having.

Senator SHERRY—There are cases, as I understand, where a ruling has been given and then there may be other facts that emerge that the tax office was not made aware of. Therefore actions will follow to gather what they regard as all of the facts; there may be a further ruling, and there may even be actions resulting.

Mr Wachtel—We have positions, Senator, where we might enter into a deed of settlement with the tax office on a variety of issues. We will always be agreeable to a clause in the settlement document which states that if the tax office became aware of other facts in the future which impact on the settlement, we always respect the right of the ATO to revisit their position.

Senator SHERRY—That is why I was a little puzzled by that first sentence where you say the ATO is sometimes too oriented towards fact finding. I would have thought it absolutely basic to have all the facts which it can to make a satisfactory ruling.

Mr Wachtel—Senator, the reason we emphasise that point is that if one is looking at say a greenfield project in any state of Australia, when one goes for a ruling and one wants to sign off that some of the anti-avoidance provisions in the leasing area do not apply—more particularly part IVA does not apply—at that particular juncture you do not necessarily have every single document and every single fact because one is dealing with a transaction which still has a certain level of evolution in front of it. So one goes to the tax office for a ruling to see whether the structure that you envisage using is not going to fall foul of the anti-avoidance provisions.

The main thrust of our submission was that often we find it can be very difficult to get a ruling because it is not possible to provide the level of factual detail that the tax office might want at that stage. As a result, a taxpayer might not go for a ruling or the request for a ruling is withdrawn, and that leaves a certain level of uncertainty.

Mr Stolarek—It is principally relevant, Senator, in transactions that are at an early stage, for instance, if someone is building some manufacturing facility or starting a new business. The key issues are issues of principle and oftentimes the facts are changing, the financiers are changing their arrangements, et cetera, and the facts keep moving around and the key elements are—

Senator SHERRY—Sorry, if the facts keep moving around and there are new facts being established, surely you would have to wait for these new facts to emerge in order to give a satisfactory ruling.

Mr Stolarek—That is potentially one way of approaching it. The other way, which we applaud, is that the tax office in some areas, notably the Public Infrastructure Unit, is able to give indicative statements of opinion. This allows the communication of the policies, Senator, in a way that does not bind the tax office, or allows the tax office to review the issue at a later point in time but it gives the tax office an opportunity to communicate its policy as to the guidelines of what is acceptable. What then happens is that at a later point in time, when the final transaction has been assembled, it is possible to consider a formal binding ruling, if that is necessary. Our point to the committee was that the communication of policy on the part of the tax office in a way that does not expose the tax office to the risk of that communication being abused is an advantage because it levels the playing field and the taxpayers are all aware of the guidelines and the policies.

Mr Wachtel—An example might be that a particular security instrument could be a convertible note. What you want to do is get a degree of comfort from the tax authorities that the particular instrument you are using would be respected in its form and the interest would be deductible. I think what Tony was getting at in the submission was that what the taxpayer is looking for is a response in principle to the particular instrument at hand, but our experience is that the tax office, once again because of the very wide anti-avoidance provisions, is not willing to provide an in-principle response because the anti-avoidance provisions could totally detract from the person's original opinion.

If the facts change later, it is quite appropriate that the tax office should have the right to totally change their view, but the emphasis here was more that one often looks for a view in principle on a particular matter. In our country it is quite hard to get that because of the way the tax system in part IVA operates. That can be a hindrance at times to major projects. It is a great pity that, in the last three to five years, one of our major projects ended up in court over a tax uncertainty issue. It is not a good advertisement for us as a country.

Senator SHERRY—But if they give what may be a preliminary ruling and the facts change so that there are new facts—not facts that have been hidden but because the nature of the project or the instrument changes over time, they then have to revisit it—I would have thought that would be difficult for your clients as well as being difficult for the tax office. It makes the situation less certain. It adds to uncertainty, I would have thought. That is why I would argue that having command of as many of the facts as is possible is extremely important.

Mr Wachtel—We totally agree with that. If I could speak on behalf of the clients, what they would say is they would like to compress the time frame whereby they can get the attitude of the tax office to a particular facet of the transaction. To them that is key.

Senator SHERRY—I understand that but surely there must be examples where clients are reluctant to provide all the necessary facts, and will only have themselves to blame for the time it might take to come up with a particular ruling.

Mr Wachtel—If a taxpayer was not providing all the relevant facts which were available and that caused a problem, I would totally agree with you.

Senator SHERRY—You said earlier the tax office would more profitably spend its time in improving the law. I just make the point that I do not think that is their role, it is the parliament's role, and they can make recommendations. But in the area of trusts and particularly charitable trusts, do you believe those vehicles are used inappropriately in order to minimise tax. Or, in more extreme form, are they used in fraud? Deal with the first issue first, the minimisation of tax.

Mr Stolarek—We can perhaps comment on trust generally. We do not operate in an area where we see much of charitable trusts.

Senator SHERRY—Does your firm have any dealings with respect to charitable trusts?

Mr Stolarek—One of our partners is involved with the Australian Institute of Philanthropy. One hears occasionally about the use of charitable trusts but we are not involved in the creation of private charitable trusts by private taxpayers in any material way.

Mr Wachtel—We might have clients who are great philanthropists but we have not, to my knowledge, been involved with any.

Senator SHERRY—No figures of great philanthropy come to mind that have been discussed within the firm?

Mr Wachtel—I am not sure if I understand the question.

Senator SHERRY—No, if you do not understand it, that is fine. I am just reminded of something that I heard earlier.

Mr Stolarek—Senators, I was in fact involved with activities for a school and we were aware that the entire regime dealing with charitable trusts was amended some two to three years ago. Clearly there were abusive practices happening but, just to reiterate, we have no practical client awareness of such activities.

Mr Wachtel—The best words to use are, 'We are not subject matter experts in the use of charitable trusts,' whereas with trusts generally we might be able to help you.

Senator SHERRY—With regard to trusts generally, do you think there is abuse, misuse, that the law should be enhanced, improved, or there should be a crackdown, that at least some trusts are not being used for the original intended purpose?

Mr Wachtel—Can I link that question to comments in point 6 in our submission. I had some difficulty with the tax office identifying a particular group of people as a target, audit or hit list. It did not sit well with me from a democratic point of view to describe a particular group of people by reference to them being on 'the rich list' et cetera. I think this whole area of the use of trusts does sometimes get muddied by a level of emotion between both the tax office and the private sector. I have been practising tax law in Australia for

about 16 years. I have practised in two other countries. There was not the same level of emotion involved in this whole question of the use of trusts elsewhere.

Senator SHERRY—But is there the same level of use of trusts as there is in Australia in other countries?

Mr Wachtel—I think that is something we have actually looked at in our report.

Senator SHERRY—You have worked in two other countries.

Mr Wachtel—Yes.

Senator SHERRY—My understanding is that there is a greater level of use of trusts in Australia than most other countries.

Mr Wachtel—There might be, but let me say that if one looks at the US one can get the same effect as a trust in Australia by using a corporation which is treated as a flow-through vehicle.

Senator WATSON—Do we have the same number of flow-through vehicles?

Mr Wachtel—We do not have flow-through vehicles in this country. We have partnerships, joint ventures, and trusts. A trust is a very effective vehicle for a family to conduct a business in. It is also a very effective vehicle to protect legal liability and there are various other reasons why taxpayers use trusts.

Senator SHERRY—Yes, I understand that, but it appears to be—and this is the issue I am getting to—a very effective way of minimising tax.

Mr Stolarek—Not really. Perhaps just to amplify Michael's comments, Senator Sherry—

Senator SHERRY—Not really?

Mr Stolarek—A trust is really a taxable entity. Many of the same outcomes from a tax viewpoint that arise from a trust can emerge, Senator, from creating a family company and so on. A trust and indeed a family company in Australia are treated as separate taxpayers from the individuals. The key advantage, Senator, of a trust over a family company is that under today's tax law—the subject of the Ralph review—a trust can actually distribute capital to beneficiaries without attracting taxation, whereas a company is permitted to distribute capital, but only the original paid-in amount. Anything over and above the paid-in capital is treated as a dividend and is taxed. That is a matter obviously which is receiving attention currently and we are all waiting for—

Senator SHERRY—We are all waiting as well. I am interested in your view as experts in the area about whether or not there should be changes in respect to the law affecting trusts and their operation and the opportunities that are currently available in some areas, on some of the evidence we have received, for the misuse of trusts for tax minimisation.

Mr Wachtel—My response would be that where there is misuse, if one could more specifically target what the misuse is and legislate accordingly, that is a preferable option. You were surprised by Tony's response when you asked, 'Are trusts used for tax planning purposes'? I forget the words you used.

Senator SHERRY—Tax minimisation, tax evasion and, in some cases, prima facie, fraud.

Mr Wachtel—Yes. If there is fraud then every piece of law that we can use should be used on anyone who commit frauds—taxpayer, company, trust, whatever—no question. If there is tax evasion, my response is identical. If there is tax evasion, one should use the powers of the tax act and other criminal acts to ensure appropriate action is taken. The debate about trust is, in my view, what are the boundaries of tax avoidance? That is somewhat removed from the issue of tax evasion and fraud.

In the context of tax avoidance, I would say companies are also used for tax avoidance. Partnerships are used for tax avoidance, joint ventures are and trusts are.

Senator CHAPMAN—When you talk of avoidance, you are talking about legal minimisation.

Mr Wachtel—Absolute legal minimisation. What we would debate, Senator, if you have different people before your committee, is what the boundaries are. But if a trust were being used for a tax evasion purpose we need not treat the trust as a company to attack that. To me, in 1999, if we do not have the machinery in this country to deal with tax evasion, that would surprise me. Why would you treat probably hundreds of thousands of trusts as companies if that were the issue? I would suggest to you that is not the issue. I do not think the issue is fraud. I do not think it is tax evasion. If that exists and that is the margin, then we applaud the commissioner in pursuing that.

But in the context of tax avoidance, we do have, I think, a fairly wide spectrum of opinion as to at what point in time, or what point in the spectrum, legal tax avoidance becomes offensive. I think one of the great pities which has transpired—and it is not just over the last few years, it existed probably a decade ago as well—is that there is a great degree of emotion, both from a tax office point of view and the private sector. If comments are made publicly that a particular list of people are going to be scrutinised because they were on 'the rich list' that evokes a very valid emotional reaction, because that is not a basis for applying the law. On the other hand, if the tax office perceive that most of the abuse is occurring at this very high net worth end, then what is the specific abuse, and why do they not attack that?

Senator SHERRY—Again, time is pressing. I wanted to just conclude with this point. You were talking about loopholes and opportunities in your opening remarks and I think you used the words, 'They're available to every taxpayer who is resourced.' This comes back to your earlier comments, but is it not fact that the considerable majority of taxpayers are not resourced or do not have the same opportunities as people who are very wealthy? So I put it to you: is it not quite legitimate for the community to be concerned when what appears to be a small number of people who earn high incomes pay very little tax? Shouldn't the

community be concerned at that, and the vehicles used, because they don't have the opportunity to do that? Doesn't that undermine confidence in the equity of the system if those sorts of issues are not pursued?

Mr Wachtel—I would say the concern is legitimate but it is the same as media articles about the rate of tax a particular company pays, and journalists attacking a particular company because they have a low rate of tax. The reasons for that could be as basic as gearing up to purchase a business in a corporate context. In the context of some of these high net worth families or investors, if they similarly are geared up to purchase a building or a company, then what you end up with under our tax law is a low rate of effective tax.

One of the other problems about the holistic approach towards trusts is that we tend—I am generalising—to focus often on people whom we might classify as being more entrepreneurial. If there is a correlation between those people and the use of trusts, that might be purely a function of, as you say, them being able to afford to work out how to structure their affairs—a corporate trust or whatever—but is it appropriate to attack the use of a legal vehicle in the hands of what I would call the entrepreneurial Australians because of a perception that those vehicles are being used for a tax avoidance purpose? It is basically attacking something without having all the facts.

Senator SHERRY—I will just conclude on this, and it is a comment more than a question, but it depends on your definition of 'entrepreneurial' and what they are adding. That is highly subjective.

Mr Wachtel—Sure.

Senator SHERRY—Some of the individuals that are not paying a great deal of tax appear to have been gearing up for a hell of a long time and their net worth is going up and they are not paying very much in tax. That is the way a lot in the community see it, and that is undermining confidence. But we could debate it all day, and time is short.

Mr Wachtel—Senator, I think your example is a great example, because if a particular person is prepared to keep on gearing up and buying more buildings and buying more businesses, then I have no problem with that person getting an interest expense deduction if the interest income is returned in the hands of the Australian bank. Now, if things go well, that person is going to end up with more income.

Senator CHAPMAN—I note in your submission you comment on the tax office's role in policy issues and you give some examples here, the assertions to the parliamentary committees in relation to trust loss measures, and I think you also referred later on to taxation of dividends and the 45-day rule, limited recourse debt rules and so on. Do you believe that in its involvement in policy issues the tax office tends to blind the responsible ministers with science a bit, or snow them in terms of the legislation that is put forward?

Mr Stolarek—We think that is actually a risk. We agree with the Senator's earlier comment that really the setting of policy is at the end of the day, or the legislation is a matter for parliament. Our perception is that one of the real concerns is that there are not in fact large numbers of members of parliament who are sufficiently experienced in the

issues—as the senators here—to be able to analyse submissions that are being put to them. As you say, that therefore does cause a risk, particularly in our experience with members of cabinet who have a large number of matters to deal with. It creates the risk that members of cabinet, when given intricate tax laws, are not resourced or staffed well enough to explore all of the detailed issues.

We do not put it in the sense that the tax office blinds the minister involved—like any other arm of government—but tax laws, because they relate to emerging business, really need a strong team of advisers within a minister's office to analyse those and to discuss them with the business community. So because tax ministers—

Senator CHAPMAN—Advisers independent of the tax office?

Mr Stolarek—Ideally independent of the tax office, yes. In our experience, typically the ministers responsible for tax usually will have only one or two advisers and, because of the sheer volume of tax law coming out, we wonder whether that is enough.

Mr Wachtel—Can I just add, Senator, that the level of complexity is such that I am not aware of anyone trying to do what you asked. Just take the debate between myself and Senator Sherry about trusts. One could spend two weeks, with very valid comments on both sides, without coming to an ultimate resolution. If someone is given half an hour to posit the reasons for a particular approach to a change in taxation treatment with a particular minister, it is a very tall order.

Senator CHAPMAN—You also comment in your submission that there are instances where ATO auditors focus on raising revenue rather than a correct interpretation and application of the law, and I think you actually refer to this attitude on the part of auditors that taxpayers are automatically tax cheats. On the other side of the coin, do you think that the involvement of auditors with clients of the tax office in doing these sorts of assessments can lead to the sort of relationship between the auditor and the client whereby they might reach a settlement rather than moving to a prosecution situation?

Mr Wachtel—Reaching a settlement to avoid prosecution or reaching a settlement on the tax principles which maybe ought to have been litigated? I am not sure what you are getting at.

Senator CHAPMAN—To avoid a prosecution where another might have the view that a prosecution was warranted in a particular case, but the auditor agrees to a settlement rather than proceeding down the prosecution path.

Mr Wachtel—We could not comment on that. I cannot think of any meaningful experience that would give a proper answer to that. I suppose the people to ask that question of are those at the tax office. The fact that I cannot give you a substantive response may be evidence that I am not aware of it being the case, but I do not know.

Senator WATSON—You indicated a preference for a commission or a board to run the tax office. Do you think the term of the commissioner is appropriate at seven years, and what should be the composition of that board or commission?

Mr Stolarek—We have not thought in depth about the term. Seven years does seem to give some advantages in terms of consistency, but seven years is a long time even in political terms. The composition of the board is a matter that we have thought about in a bit more detail. We would believe that the board needs to have businesspeople and members of the various stakeholders in the tax office—that is to say, potentially some representation from community associations, et cetera. But it should have a significant complement of businesspeople and tax academics and professionals.

We would see the role of the businesspeople being to add direction and to have the capacity to champion the tax office, because we do believe that a lot of the solutions that we have discussed—the resourcing of the tax office, change of focus, et cetera—will require an interface with the government and an interface with the business community in order to change the perception and to change the focus of the tax office. We see the board of the tax office being constituted perhaps differently to some of the other government authorities in having a stronger focus of taxpayers and businesspeople who are charged with assisting the tax office to focus on its key strategic challenges, the key changes in business that demand action, and also to assist the tax office in focusing its activities to get maximum efficiency and effectiveness.

Senator WATSON—What should be the size of the board in terms of numbers and should there be a government or a parliamentary representative on that board or commission?

CHAIR—You might like to take that on notice.

Mr Stolarek—Yes.

CHAIR—You also might like to take account of the submission put to us before from the CPSU with regard to the setting-up of a commission, not dissimilar to what Senator Watson is asking about. It would be useful for us if you were to look at that and then present to us in writing your own views about that and how it might operate. That might prove to be quite helpful.

Mr Stolarek—Thank you.

CHAIR—There are no further questions. Mr Wachtel and Mr Stolarek from Arthur Andersen, thank you. I apologise for the fact that we are running late. We will now take a short lunch break and resume in camera.

Proceedings suspended from 12.55 p.m. to 1.44 p.m.

Evidence was then taken in camera, but later resumed in public—

[4.28 p.m.]

LAPIDOS, Mr Jeffrey, Secretary, Taxation Officers Branch, Australian Services Union

MEYNELL, Mr Keith Albert, President, Taxation Officers Branch, Australian Services Union

THORBURN, Mr John, Member, Australian Services Union

CHAIR—I welcome the officers from the Australian Services Union. Do you have any comments to make on the capacity in which you appear today?

Mr Lapidos—Yes. I am also an employee of the Australian Taxation Office.

Senator WATSON—What area?

Mr Lapidos—I work in the receivables management area of small business.

Mr Meynell—I work for the Australian Taxation Office.

CHAIR—In what area?

Mr Meynell—Currently, I am in sales tax technical advice.

Mr Thorburn—I am an ex tax officer. I retired in June after 37 years service and I worked in LB&I, in the larger end of town.

CHAIR—Thank you. The committee prefers all evidence to be given in public but under the Senate resolutions you have a right to request to be heard in private session. Before we proceed, I also draw to your attention the nature of this and other Senate committee inquiries. Senate committees do not have the power to make determinations or orders and do not function as a dispute resolution body. Without pre-empting the committee I point out that, based on past practice, it is unlikely the committee will make recommendations on individual cases; rather, it is expected the committee will explore a number of individual case studies in order to draw a conclusion on the general systemic issues in the operation of the ATO.

Because of this, the committee wishes to avoid receiving evidence that constitutes adverse comment about individuals as far as possible. If you wish to refer to an individual adversely, then you should be aware that the committee is obliged to extend a right of reply so, wherever possible, you should refer to them as Mr X or Ms X. If you do wish to refer to an individual by name, I request that you advise us first so we can consider whether we should proceed in private session. I now invite you to make an opening statement and then we will proceed to questions.

Mr Lapidos—Briefly, I wanted to comment on something that was said by the CPSU this morning, particularly in relation to the idea of a management board sitting on top of the Commissioner of Taxation. We disagree with the CPSU and I have difficulty understanding

where their view comes from. We would have very grave fears if the independence and integrity of the Commissioner of Taxation was compromised—and we believe it would be if there was a management board sitting above the commissioner. I think it is important for the Senate to understand that effectively all the tax office's powers are vested in the commissioner and all his officers exercise his powers through a system of authorisations and delegations.

If there was a management board which sat above the commissioner, which had its membership drawn from the professions or the business community or even from community groups, they would be in a position to direct him in the way he operates, which means effectively that they are directing us as officers of the commissioner in the way that we operate. All of us are covered by the Public Service Act and there are provisions about conflict of interest. We are not allowed to have conflict of interest. If we are working somewhere else we have to get permission from the secretary—all those sorts of things. That would not apply in the case of a management board.

So you could imagine a firm of lawyers would love to have a representative who would be in a position to know what the commissioner knew so they could direct the commissioner; the same with a firm of accountants or business people. We believe that the confidence of the staff would be substantially shaken and the confidence of the community would be shaken if the independence the commissioner has was shaken. The CPSU indicated that the term of office for the commissioner of seven years was too long. We do not see any reason to reduce the term of his office; in fact, I would suggest that the government should reappoint a commissioner, unless they have substantial reason not to reappoint. If they are not going to reappoint him, then they should put appropriate weight on his recommendation for a replacement commissioner.

The independence of the commissioner is absolutely integral to our system of taxation and I can only urge you to respect that independence for the central place it does have in our taxation system.

Senator WATSON—I think it would be helpful in relation to certain types of issues such as the evolution of rulings.

CHAIR—Could we complete the opening statement first. I will also say that we are somewhat short of time, but that is our fault because we have been running overtime. We will be back in Melbourne, so if we get to a point where we have not finished, we will obviously come back.

Mr Lapidos—The other thing I would like to say in terms of opening is that Mr Thorburn, on my left, has a wealth of experience in audit and the issues of access powers and other issues that have been raised with you in fact earlier today. You might care to raise these issues with him. We were talking earlier about charitable trusts; he has knowledge of those things and a lot of other areas. Keith Meynell, on my right, has a lot of experience in the withholding tax area of the office, as well as now in sales tax. I tend to talk to a lot of people and find out what is going on. You have seen our written submissions, so perhaps I will leave it to you to ask any questions now.

Senator WATSON—Would you like to comment on what you have heard today—in particular, tax officers going to work for the private sector? You sat in on the hearing.

Mr Lapidos—We raised one part of an issue in relation to tax officers working. I have become particularly concerned because of reports that we received in relation to transfer pricing in the international part of LB&I. I do not know if you are aware of the EL2 level in the public service, in the tax office, but they are senior officers who earn roughly $65,000 to $80,000 a year. It depends on exactly what their level is—but that sort of money level. They are just below the SES.

There is a group of about eight people there who have been developing the transfer pricing policies of the office, developing the rulings. They have been involved in public education with the big companies that are involved in that transfer pricing. What has happened is that numbers of them have been approached by the private sector for employment and numbers of them, I believe, either have left or are about to leave. They have been offered salary packages well in excess of what the tax office can compete with. I spoke to one of them to find out the general level of the package that was offered and it was up around $125,000 to $130,000 a year, plus full salary packaging, relocation assistance if it was required, and the promise of heading towards a $160,000 salary package within a few years if everything works out. The tax office is just a million miles from what these people can earn.

You were talking about a different sort of thing this morning—once they get to the private sector, whether they get some advantage for themselves. John would probably be in a better position. I have not heard of anything that would be of any concern, nor in relation to organised crime in all my time. I have never even heard whispers.

Senator WATSON—I was not suggesting organised crime. I was suggesting there is the opportunity for networking to get particular advantages.

Mr Lapidos—I network within the tax office as a union official.

Senator WATSON—That is right.

Mr Lapidos—And there is nothing wrong with that. People will network.

CHAIR—We are talking about ex tax officers being employed in the private sector.

Senator WATSON—Being paid to network, effectively, within the tax office to get a particular advantage.

Mr Lapidos—It depends on what they ask people to do for them.

Mr Thorburn—I am not aware of any major dramas with the networking. It does go on, I am sure. People ring up their old friends and talk to them. I am not sure whether they are asking for any favours. As far as I know, once people leave, if they do ring up it is just informal but it has nothing to do with work. We do not relate it to work. I have never had anyone ring me and ask for any favours. If they did, they would not be getting them. I do

not know of any of these networks going off the rails, but I am sure there is a possibility that it could happen.

Mr Meynell—I think we would have to make a distinction between expediting a matter and gaining favourable advantage.

Senator WATSON—Yes, we have done that. I am talking about technical matters.

Mr Meynell—There are plenty—and obviously networks are maintained—and in terms of expediting matters I know for a fact that certainly goes on.

Senator WATSON—That is not a problem.

Mr Meynell—I am not aware of any of the people at a senior level who have left and gone to the private sector interfering or trying to gain favour on a particular matter they have raised with the office. I think that would be nearly the position I would expect of every officer within the Australian tax office.

Senator WATSON—Are there any protocols for people who are employed in the tax office for when they leave, what they can do or what they cannot do or how they can use information?

Mr Lapidos—I do not believe there is anything that binds us once we leave. I beg your pardon. Section 16 of the Income Tax Assessment Act continues to affect people after they leave.

Senator WATSON—Yes, that is secrecy and all that, isn't it?

Mr Lapidos—That is right. I suppose to some extent the privacy legislation does the same thing. But if you are talking about working in an accounting firm, the fact that you know something, there is nothing really that forces you to empty your mind of it. The law cannot reach in that way.

CHAIR—I would like to ask a few questions concerning the issue of the LB&I and the communication between, say, senior management and officers actually at the coalface doing the work. There have been some claims that there is a lack of communication between staff and management or officers and management and also a lack of communication with regard to matters between units—that is, say, the LB&I in particular and the PIU—the Prosecutions Investigation Unit. Would you like to comment?

Mr Thorburn—The way we are structured, we have got different segments within LB&I, and a lot of the leadership, the segment heads, are spread around the countryside. For instance, you may be working in Box Hill in the manufacturing area and your head may be in Sydney. So there is a problem with distance. You do not get to see your leaders very often and there is a lot of emailing and messages but it is all very distant. Fortunately, when I was in Box Hill my segment leader in charge of the whole area—which was super and insurance—was in the same building and it was much better to operate and work directly

with him on site. But there is difficulty in communication because of people being all across the countryside.

CHAIR—Do you have a view in relation to the evidence which has been submitted to us that there is reticence on the part of LB&I officers to proceed with prosecuting large tax avoidance situations; rather, they have sought to negotiate them out for settlement?

Mr Thorburn—Yes, there is a tendency for that.

CHAIR—Why is that?

Mr Thorburn—If you have a breach of, say, a 264 notice and you go to the prosecutions area, they are prepared to take it on board and ask for a court order and do some of those things. But if there are more serious things, everyone is a bit more reticent to move forward with them and we always try and resolve them without prosecution. There does not seem to be a big emphasis on prosecutions nowadays.

CHAIR—Should there be?

Mr Thorburn—I think there should be, yes.

CHAIR—Are you taking into account some of the evidence that has been presented to the committee, like a tax obligation of a billion dollars and only $60 million was paid—that sort of thing?

Mr Thorburn—Yes. It is difficult to get the evidence for a start. If you are going to do a prosecution you have to get the facts and the evidence and we run into obstacles with legal professional privilege and accounting guideline restrictions.

CHAIR—This is section 263 and 264?

Mr Thorburn—Section 263, access, yes, and 264 is requiring information by correspondence.

CHAIR—Do you have any view about that as a piece of legislation and whether or not it ought to be changed?

Mr Thorburn—I think 263 reads very well but in practice it is not working as well as it should. We are running into obstacles with blanket claims by the legal profession and the big corporates in particular, of information and records for which they claim professional privilege. They tend to attach a lot of additional information under the letterhead and the lawyers will write a bit of a memo and, quite often, in-house lawyers, to say, 'Well, the in-house lawyer dealt with that file; therefore all of that paperwork is privileged and you do not have access to it.' Unless you get access to a lot of this planning information and the factual information you cannot work out how these avoidance arrangements are working and you run into brick walls.

Instead of a case taking six months or 12 months to finish, it is rolling on for years running into brick walls. You find thousands of documents put aside. They give you a list showing what documents have been put aside under the guidelines. The list is usually bland and difficult to interpret. It is always under their control and they tend to set down what they want to put in the list. It is vague and you usually cannot make a judgment on the paperwork supplied. If you want to challenge these things, you have to go through a lengthy procedure. You have to go to AGS. You have to argue whether the list needs to be revamped and get a better list. Then they give you a better list and you say, 'Well, some of those shouldn't be privileged. We want those put aside.' We have had a few cases where we have challenged them and some of them were not privileged and they had put them aside under a blanket protection. But most of them just hit brick walls and the cases flounder.

Mr Lapidos—Senator, on the question of an amendment, what we would propose you look at is an amendment which basically says that 263 and 264 override legal professional privilege. The words of the rest of the sections are okay in our view. Effectively the privilege or the pseudo-privilege that has been extended by the Commissioner of Taxation to accounting papers was given to provide some equity between accountants and lawyers because the accountants argue to the commissioner, 'How can we compete with lawyers if they can withhold all this documentation from auditors? All our clients will prefer to go to a lawyer and we are going to lose business.' So it was a business competition sort of argument. While we can appreciate the place of legal professional privilege in the general community, it is effectively being used to frustrate the tax officer's ability to assess taxable income and to amend.

Senator SHERRY—Would you support its abolition?

Mr Lapidos—In tax matters?

Senator SHERRY—In tax matters.

Mr Lapidos—Yes.

Senator SHERRY—In your experience does it tend to be the higher income, higher wealth individuals and companies, the trusts, whatever?

Mr Lapidos—They are not the only ones that try it on, if that is what you mean.

Senator SHERRY—That is what I was going to ask you, yes.

Mr Lapidos—No. I have had personal experience of it at the individual level, quite low down. This is a case that was quite some time ago, they tried it and I spoke to one of John's former colleagues and had some advice about how to deal with it. We just out-bluffed them, I suppose.

Senator SHERRY—Is it widespread at the upper income level?

Mr Lapidos—There is a lot of documentation within the tax office, which the committee could ask for, which is referred to in our submission. They have set up an information network. Is that what it is called?

Mr Thorburn—There is an access network that has been set up in the last two years. It covers the northern region and the southern region and it is endeavouring to try and help the auditors with their access problems. It is all very nice on paper but it has not progressed much at all. They have flagged the problems. They have identified and said, 'Yes, we know there's a problem. There is a big issue there but what can we do? The law is the law. LPP restricts you. What can we do?' There has not been any big success through that network because it gets up the top but it then runs into lack of willpower and difficulties with people saying, 'Well, really the next step is to go to government, but no-one is going to do that.'

Senator SHERRY—Why is no-one going to do that?

Mr Thorburn—Because people say it probably is not the right climate or something. People do not go forward with the problem. The problem sits and it is not progressed as it should be in the eyes of the auditors.

Senator SHERRY—I was asking earlier about how widespread this is amongst the higher wealth individuals.

Mr Lapidos—It is a really big problem in the higher wealth area.

Senator SHERRY—And lower down?

Mr Thorburn—Yes. It covers the lower ranks as well. There are pockets of middle-ranking businesses who utilise good lawyers and have good accountants and they know how to protect themselves from access. It is very widespread with the big corporates. They have it in house. They have their in-house groups. They are well set up and well equipped. It has all developed in the last nine or 10 years. It has taken us down this path. There was a bit of a watershed with the Citibank reign back in 1988 when all the big corporates got nervous after we went to Citibank. They said, 'We'd better pull close together and get a brick wall up here and unite ourselves.' They have now made it very difficult for us to progress our work.

There was a Professor Sue McNicholl contracted by the office to come in and examine legal professional privilege and the effect on the office. She has been around in the last 18 months and has drawn examples from each office of difficulties.

Senator SHERRY—Is she issuing a report?

Mr Thorburn—There is a report that is supposed to be finalised, I would say, by now. It was to go to the commissioner, I believe. She interviewed me and she interviewed a number of people and took the case studies that we had to explain to her. She was appalled at some of the stories and said, 'How can you people operate under this regime? No wonder you are hitting brick walls. You're just getting nowhere and it's not efficient to be operating in this way.'

Mr Lapidos—You heard the accountants this morning talking about the desirability of transparency in the tax office, but we want some transparency the other way around. In fact, on the issue of transparency, the tax office has taken advantage of information technology developments and invested a lot of money into developing systems and making them accessible to the private sector as well. That has a bearing on consistency of decision-making and there are whole stacks of systems available to tax officers and the public where case law is put there and it is accessible. There are search engines and things like that, all in the interests of promoting consistency in decision-making, to promote transparency in decision-making, to make sure the private sector are aware of all these things. But it is not a two-way street because when it comes to their clients' dollars, accountants and lawyers make that their first interest to minimise their tax bills.

Senator SHERRY—That is what they are paid for.

Mr Lapidos—That is exactly right. We, the tax office, cannot raise the money that you, the parliament and the government, need to spend to advance the interests of the people of Australia. We cannot properly raise the revenue in an equitable way without proper powers to be able to assess what people's tax liabilities are. That is what we want to be able to do. I was speaking to Jim Killaly who is in charge of large business and income a few months ago and he was saying, 'Well, cases are taking too long.' That is right, we concede that. He was talking about what he did and I do not know if you have had an opportunity to speak to him recently, but it probably would be a good idea.

He, for some reason—I do not know why—became involved in one particular case where there was an overseas transaction of $3 billion for one transaction. I do not know who the company was, presumably some multinational company, but the entry that he looked at was basically that $3 billion went into the cashbook and $3 billion went out. There was no supporting documentation for the transaction so he issued a section 264 notice to require people to attend and give evidence and things like that. He hired lawyers to assist him with the questioning of the people that knew about it. He indicated to me he was prepared to go to the Federal Court, if necessary, to seek a declaration if there was a question about whether questions should be answered or not and documents produced or not.

The problem is it is all very well for a first assistant commissioner, which is what he is, and a national program manager to say, 'Well, I'll get involved. I will look at this particular transaction. I'll bring people before me. I'll examine them on oath and I'll get lawyers to assist me. I'll rush off to the Federal Court, if I need to.' But he is not the one that is usually doing the work. I was very surprised that someone so senior got his hands dirty, if I can say that in an appropriate way. What we need is for people well below him to have a system in place where they can enforce the law.

We were talking before about how a system could be made to work, so we canvassed the idea of a special tax court where access issues could be quickly litigated. An auditor needs to be able to deal with issues quickly. The taxpayer really should have an interest in matters being done quickly. In fact, what happens is they have got an interest in it going on forever because, as soon as the four years are over, effectively we cannot audit any more. Every year that drops off, so many millions of dollars are potentially gone. If legal professional privilege had to remain, we would say we need effectively a judicial forum because they are the only

people who have the power to make decisions of this nature. We can pop in and see a master or something like that, and say, 'These are the documents. Let's have a debate about whether they really do attract privilege or not,' and it is something that can be happening quickly.

I know this from speaking to the new Tax Council or whatever it is called. Michael Bersten is on the new Tax Council. I have forgotten his correct title. He was saying to me a month or so ago that the litigation area of the tax office, which is his responsibility, has had its budget cut by about $4 million or $5 million. This is a problem for the office. These were anticipated savings from bringing litigation areas together under one roof rather than being spread out amongst the business lines—consolidating them. I have a concern about whether the office has got sufficient funds to properly litigate issues.

I do not have anything in particular where I can say, 'This case wasn't litigated,' when it was, but if you listen to John, if you look at what is happening in the access issues you will see that the staff do not have the confidence or a procedure whereby they can, with confidence say, 'Look, we need this information. We can do a case quickly, if we've got it.' They should effectively be able to knock on the door, introduce themselves and, with reasonable notice, be told exactly what the tax issues are that need to be reviewed, rather than having to work through a maze which has been developed specifically to make sure that they do not find things. It is just making it impossible.

CHAIR—That ultimately is probably something that has to be addressed through legislative mechanisms.

Mr Lapidos—Probably. It is legislative and it is resource driven as well. The two go together.

CHAIR—Absolutely. But if you are shrinking the resources then you also have to make the legislative processes such, I think, to accommodate them.

Mr Lapidos—Yes. I know that some of the wealthiest people in the country pay effectively no income tax. I am not going to say who they are. I probably should not have been told who they were in the first place. I have not been given details but when you hear that someone in the top 10 pays virtually no income tax, it is just shocking. People do not know. I cannot tell them, the auditor cannot tell them, the tax office cannot tell them. If the ordinary people in the street knew that one of the top 10 wealthiest people in the country paid virtually no income tax, it is just unbelievable.

Senator SHERRY—You do not believe the excuse of entrepreneurship is sufficient to justify that?

Mr Lapidos—Absolutely not. To suggest that it is because people just keep on reinvesting and borrowing money so they can reinvest and just by negative gearing, it just beggars the imagination. If that was the process, it should not be available to them. I am sure that is what the people would say. That is what I think.

Mr Meynell—Negative gearing came and went and then was reintroduced.

Senator CHAPMAN—If they are borrowing and reinvesting and creating business activity, if it is a genuine activity.

Mr Lapidos—I accept in principle the hypothetical example but there are issues of tax equity. What I am suggesting to you is that if people could see that someone in the top 10 wealthiest people paid effectively no income tax simply because of the way they structured themselves, even if they were investing and there was some argument it was for the benefit of the community, people would still, I believe, just not accept it.

Mr Thorburn—For example, the small business entrepreneur who is paying tax would not have the same opportunities, presumably; some might.

Senator CHAPMAN—What you are saying if it is some contrived scheme—but if it is purely borrowing and investing therefore they are not actually getting—

Mr Lapidos—It is all hypothetical anyway.

Mr Thorburn—But it is not as simple as that. They are usually very contrived arrangements. They have multiple trusts and all these things.

Senator CHAPMAN—Yes, sure. I said excepting that, but you just gave a simple example of borrowing and reinvesting.

CHAIR—But also I think our point here that we are investigating is this issue of access to information.

Mr Lapidos—That is right.

CHAIR—Which is also used, as I understand it, for the purposes of possibly avoiding the payment of tax.

Mr Lapidos—Yes.

CHAIR—That is the issue that I would like to address, and it is an important one that we have to address. It goes to equity treatment across the spectrum of taxpayers of this country.

Mr Lapidos—Ultimately, the Commissioner of Taxation has expressed concern about the access issues. We are not privy to what he has been saying to the government at all. He has only spoken in very general terms publicly. We know that he has engaged the consultant John has referred to. I would urge you to speak to him about it.

CHAIR—We will be, rest assured.

Mr Meynell—I would just say that is a problem across the board: information in general. Still the best method to avoid tax in Australia is just not to disclose. ABN will help in this area, but areas where I have had personal experience where we have done coverage projects, where we have checked the information internally against what the taxpayer has

provided to the Australian tax office and what they have provided on external databases, show in some areas of taxation liabilities that there is rampant nondisclosure. We went through the Australia card and the TFN debate but there is still the fact that you are not required to provide a TFN. You can utilise many legal processes such as legal professional privilege just not to disclose information.

I know that other issues were raised about the non-equitable treatment of taxpayers. I suppose that goes to the heart of the taxation system: that we look at equity issues and everyone should be on a level playing field. But the fact is that if you have proper advice and you are privileged to information that the average run-of-the-mill person in Australia does not have, then you do have an advantage. A person who is just an average salary and wage earner has no avenues to not disclose because their employer is going to issue them with a group certificate. The government has even gone to the extent of insisting that fringe benefits are placed on the group certificate.

To the average worker, there is nowhere to hide. To other sections of the community, there is, because they realise that with proper advice and nondisclosure they get an advantage. I know that we move along in these areas and, as I have said before, negative gearing is being looked at. Infrastructure bonds, tax trust lossing, franking credit trading are all things not available to the average person in Australia. I think that is something in terms of public perception on high wealth as well. We are gathering information on these and the government has responded from the information that we have collected. I think it will be an ongoing process.

We were talking about tax minimisation. Many entrepreneurs use the argument that the government does not spend its taxes so wisely that they should pay one cent more than they have a legal obligation to. It is a prevalent argument and, of course, it is going to be an ongoing evolution. They will come up with certain methods and government will respond. But on a basic question of equity, the ability not to disclose information I think is a worrying one.

CHAIR—Yes. That issue is going to probably be foremost in our questioning of the ATO and in looking at what we might ultimately recommend about what the government might do in that particular area. There are some other areas that we probably will need to come back to you about, but can I say thank you very much for appearing here and for your submission which you have put in. We would appreciate it if we can contact you if we need further information and advice.

Mr Meynell—Sure.

CHAIR—I am sorry that we were running so late. We had to cut the time a little bit shorter than we would otherwise have liked, but it has been a very interesting day.

Committee adjourned at 5.04 p.m.