



COMMONWEALTH OF AUSTRALIA

Proof Committee Hansard
**HOUSE OF
REPRESENTATIVES**

STANDING COMMITTEE ON TAX AND REVENUE

Commissioner of Taxation annual report 2018-19

(Public)

FRIDAY, 26 JUNE 2020

CANBERRA

Friday, 26 June 2020

Members in attendance: Mr Falinski, Ms Kearney, Ms Owens, Mr Thistlethwaite, Mr van Manen, Mr Young.

Terms of Reference for the Inquiry:

To inquire into and report on:

The Standing Committee on Tax and Revenue will inquire into and report on the Commissioner of Taxation Annual Report 2018-19.

Youtube audio

<https://www.youtube.com/watch?v=ukWaP6uTePA&t=578s>

PHILLIPS, Mr Ken, Executive Director, Self-Employed Australia

Evidence was taken via teleconference—

[10:43]

CHAIR: Welcome. Do you, as a witness appearing before the committee, have any objection to being recorded by media during your participation in this hearing?

Mr Phillips: No.

CHAIR: These hearings are formal proceedings of the parliament. The giving of false or misleading evidence is a serious matter and may be regarded as a contempt of the parliament. The evidence given today will be recorded by Hansard and attracts parliamentary privilege. I invite you to make a short opening statement.

Mr Phillips: I'll be as quick as I can to cover as much as possible. Very briefly, we go back to 2000 with the ATO. We've been on small-business committees since then. Around 2014 our commentary about the ATO started to become a lot more robust, although still quite polite. We were heavily involved in the *Four Corners* April 2008 'Mongrel bunch of bastards' show on the ATO. We have very significant experience with the ATO's dealings with small business and, we've got to say, those experiences are not good—in fact, they are rather bad.

Since the *Four Corners* show in particular—and well before—there have been numerous reports from the Inspector-General of Taxation, the small business ombudsman and parliamentary reviews, and I've looked at parliamentary reviews on this going back to the 1970s. There's a consistent pattern of behaviour shown in reports coming out telling us exactly what's happening with the ATO and, in our view and our experience, abuse, particularly of the small business sector, by the ATO where they simply get things very, very wrong.

I won't go through trying to prove all of that, because we've got to the stage where we've said: 'Look, there are mountains of evidence about the problem here. Where are the solutions?' What I want to do is focus the committee on one central top-end problem from which everything else flows. It relates to the ATO's powers at law. One must remember that the ATO was established in 1936 and these primary powers have not altered since 1936. The central power that creates all of the problems is that, when the ATO does an audit and forms an opinion of a debt that is owed, that opinion becomes a debt at law. It is no longer an opinion; it is a debt at law, and that debt is due and payable immediately at law. Not only that but, when the taxpayer believes that the debt is not correct, the taxpayer must disprove the ATO's position and has to go further: they have to prove the correct position. In other words, we're operating in an environment of reverse onus of proof with the ATO. The ATO, as a consequence of this, can at law, and does, collect before and during appeals and objections.

I have to tell the committee that this situation does not exist in either the United States or the UK. In both the United States and the UK, the tax collection authorities cannot collect an alleged debt until that debt has gone through the entire appeals and objections processes, including any court appeals processes. In other words, there is a very stark and distinct difference between the powers of the ATO and the powers of the IRS in the US and HMRC, the tax collection agency in the UK.

What happened is that we'd been searching around for solutions on this, because there are mountains of descriptions of the problems. In the middle of last year, in July 2019, what came across our desk was an alert on a law in the US that had just been passed by Congress and signed in by the President, the Taxpayer First Act. We had a look at this, and it was an extraordinary piece of legislation. We couldn't believe what it was, and we said, 'Well, there's something going on.' We decided that I needed to get to Washington. We raised some money, and I spent two weeks in Washington in October of 2019 doing a research project into the laws covering the administration of the IRS. When I got over there and met with people, I was told, 'No, it's not what we did in July 2019 that was important but what we did in 1998.' What unfolded from there for me was a gobsmacking revelation of the reforms to the IRS in 1998. I met with people who were on the congressional review of the IRS in 1997, which led to the 1998 act. I met with the principal draftsman of the 1998 act. I met with the senior people from the Taxpayer Advocate in the United States. I met with congressional staffers who are involved in the primary committee that oversees the IRS in the United States. I met with lawyers, tax accountants and so on and so forth.

In the United States, what they brought in in 1998 was what they called the Taxpayer Bill of Rights. It is a legislated bill of rights. It has about 10 items to it. One of those items, for example, says that a taxpayer is entitled to finality. Backing up that bill of rights are 71 legislated provisions that describe exactly what the IRS is and is not able to do in terms of the administration and collection of tax and so forth. One of those items says that the IRS cannot charge interest on a tax debt that is higher than that which the government itself pays. In Australia, by

comparison, my recollection is that the ATO charges seven per cent more in interest than the government itself pays in interest. The IRS cannot collect on a debt until all objections and appeals have been completed, including objections and appeals to a dedicated tax appeals court. The IRS has the onus of proof, and there are multiple checks and balances running through the system. They have the very powerful Taxpayer Advocate; it is the equivalent of our IGT but has over 1,600 staff. In 2006 they brought in some very significant whistleblower laws which enhanced the capacity of the IRS to collect money. Essentially, anyone who blows the whistle on a bad taxpayer is entitled to receive a percentage of the revenue raised. Then came the Taxpayer First Act 2019, which has gone further again.

In two weeks I discovered all of this, and I have written a 50-page report which compares the situation in the US to the situation here. What we're saying to the committee is that the situation in the US forms a template for the sorts of reforms that we should do, and need to do, here in Australia with the ATO. Not every one is directly transferable, of course; there are different situations, there are different tax laws, there are different cultures and there are different institutions. But, in terms of a template, this is an extraordinary situation and we have attempted to explain that clearly to give some sort of pathway through. I've got that report sitting there and we are very keen to share it. We believe it is absolutely time for us to move from descriptions of the problems at the ATO to solutions for the problems at the ATO. Those solutions need to be legislated; we should not leave it to the ATO to do the reforms themselves.

I will come back once again and do some updates for today's situation. Remember, what we are saying is that the big-ticket item here, which is the problem, is that, when the ATO does an audit and forms an opinion of a debt, that debt becomes a debt at law that is due and payable immediately and so forth. What we have had in place since last year is that the ATO issues a statement of tax record—it's a new law—and government departments can't use the services of any business that has an adverse statement of tax record. What we now have is that the ATO is the arbitrator and the overseer of 'who is allowed to have a contract with the government'. This has enormous, wide-sweeping implications, particularly when you take the situation with the powers of the ATO. If the ATO gives an assessment of a business's tax situation and gets that assessment wrong and issues an adverse statement of tax record, the ATO, on its own assessment, is able to absolutely prevent someone from doing business with government.

We now have Director Identification Numbers; these are controlled by the ATO. Again, we have a situation where, if the ATO decides to take away your Director Identification Number, whether they are right or wrong or the facts are correct or not, you are in significant trouble and basically that's the end of your capacity to be in business.

I will now turn to what is happening with the COVID situation. On 23 June, just a few days ago, the ATO issued a warning to people, entitled 'ATO zeros in on COVID-19 fraud', and has announced a very robust program of chasing fraud. The problem with this is that, once again—we come back to it—if the ATO do an audit and they believe and form the opinion that you have committed fraud, that is effectively the end of the case; they are the sole arbitrator. I am predicting a blow-up of enormous proportions here that is going to cause mayhem particularly through the small business community. I'll give you three quick examples, which I can explain in more detail should you be interested. The ATO have announced in their release that they are going after people who access the early release of super and then make co-contributions. There was nothing in the law that said that, if you had an early release of superannuation, you couldn't make an additional contribution to superannuation. The ATO has now turned around and said, 'Aha—this could be captured under the anti-avoidance mechanisms.' Once again, this will be at their whim.

We wrote to the Treasurer on 1 April saying that there was a significant problem in the design of the cashflow boost with sole traders who work as Pty's. The cashflow boost is clearly intended under the legislation to go to businesses where they have—let me call it—arm's-length employees. But we said that there's a problem here, because the cashflow boost is going to go to sole traders who run a Pty where the sole trader may be the only employee. We can confirm that that has happened across the board. People who are sole traders are getting this, and we think that the ATO will wind up doing audits of that.

We've listed a number of areas, but this is one of the other areas. The ATO have said that they'll be taking JobKeeper away for people who manipulate the turnover. We are predicting that there is going to be considerable strife in this area with the ATO's audits. This is coming back to the fact that the ATO doesn't audit and forms an opinion of a debt, and the opinion becomes a tax debt at law.

I didn't expect to receive an example so quickly of exactly what's going on. I thought it would take some months. **But, on 24 June, I was alerted to a situation of a company with 21 employees. They had applied for and received JobKeeper. The basis of the application was that their March turnover of 2019 compared to 2020 had dropped 47 per cent. If you remember, under JobKeeper, once your turnover has dropped, you are entitled to it, no matter the**

situation, for the rest of the five or six months. However, on 24 June, they had their JobKeeper cancelled on the basis that the ATO said that their April comparison—2019-20—had dropped 15 per cent. Therefore they withdrew the JobKeeper. The company have sent me all of the records in the correspondence with the ATO. I have read them. I could not believe what I was reading. The cancellation of their JobKeeper payment doesn't even reference the March turnover. That's the end of my introduction.

CHAIR: You went a long way over five minutes! We're going to extend the committee and allow for 15 minutes worth of questions. I think, Bert, that you indicated you had a question? Is that right?

Mr VAN MANEN: No, I didn't haven't a question. I was just making a comment. I thought ASIC were managing the Director Identification Numbers as part of the Modernising Business Registers Program. I'm sure the ATO has their finger in the pie somewhere as usual. I thought that was primarily ASIC's responsibility. That's all; so it's just a comment.

CHAIR: I think, in answer to that, we handed over all of the registries, of which there were 33, to the ATO for a modernisation program. It doesn't seem to me that very much is happening. As you and I have heard in corporations and financial services, ASIC doesn't view it as their job to do anything.

Mr VAN MANEN: We'll have a separate discussion about that offline.

Mr YOUNG: This is dear to my heart as a small-business owner for the last 20 years. I have been a victim—sorry, a client—of the tax department for 20 years as a small-business owner. I agree with the comments that the scope that they have is unbelievable. Quite often, when people have a tax debt, they're already in a lot of trouble. To give them the burden of the cost of an audit—and a lot of accountants now are charging audit insurance, so you pay this extra \$500 or \$1,000 a year, which is another cost to your business in case the ATO may do it. So you might be in business for 20 years, pay 20 grand in insurance fees and never get an audit, which is 20 grand that could be reinvested into your business, staff, equipment or whatever. I'm with this: I think it needs to be funded by the ATO. If they come and do an audit, I think that they should be paying the cost of your accountancy fees to do that audit.

I also agree that you should be innocent until proven guilty, because that's really what we do in this country in every other aspect. To have a penalty put on you and be accruing interest while you're going through that and adding to the burden—we talk about mental health a lot. The mental health and stress it puts on people is totally unfair.

I do have a question about the record. I haven't heard of that adverse tax record and that you couldn't do government contracts. So that's for a tax debt—is that what we're saying?

Mr Phillips: It's called an adverse statement of tax record, and I'd have to dig into the legislation to discover precisely the powers around that. But, when this was first floated under the Black Economy Taskforce review, we issued warning signals about it again, saying, 'This all depends upon the integrity of the tax audit system and the collection system.' My view would be that, if you get an adverse audit from the ATO, you will receive an adverse statement of tax record and you are then banned from doing business with government.

Mr YOUNG: I don't have a problem with people being tax cheats, to use a layman's term, and there being a penalty, but I would like to find out, firstly, the parameters around that, and, secondly, once they've rectified the issue, whether it be a debt or whatever, whether they then lose that and are able to trade with the government. I'm not sure if you know that now, but, if not, I'd like you to take it on notice and maybe come back to us with that.

Mr Phillips: We come back to the central problem: the administration of the tax system must adhere to normal principles of justice. It does not. In our view, we describe the ATO as having the powers of a dictatorship. What it says is law and to be able to move against it is very akin to Chinese-type situations. When we compare it to the United States, where there's a very sophisticated system of checks and balances to ensure that tax justice applies in terms of administration, the difference between Australia and the United States is quite extraordinary.

Mr YOUNG: I don't think you're going to get any argument from us on that, and we take that point on board. Like I say, if someone has been proven to have a tax debt and they do have that debt, I personally don't have a problem with them not being able to deal with the government until they sort that out. But what I want to know is: does that stay there forever or, once they've sorted the debt out, are they then able to? And I'm not sure about that.

Mr Phillips: You and I are on the same page. If the debt is genuine and the taxpayer is—we have no problem with it. It's the process of justice that we're concerned about.

Mr YOUNG: On that, I'd like to get the correspondence on JobKeeper because I'm in the same situation. I qualify for JobKeeper in my two businesses. We haven't been down 30 per cent since April, but we have still been getting the JobKeeper payment. I haven't had the same experience, where it's been cancelled, at all.

Mr Phillips: I've asked the company if they would be prepared to share the correspondence with the committee and, subject to them checking with their lawyers for confidentiality, they're more than happy to do that. I'll ask them and I'm quite sure they'd be happy to do that.

Mr YOUNG: Perfect. The last thing is on the cash boost. I was very interested that you said you were concerned that it was targeted towards contractors—I think you said that; it was a bit hard and a bit scratchy. Are you saying that some of them didn't get the cash boost?

Mr Phillips: No, I'm saying that there are a vast number of people—probably several hundred thousand—who will have received the cash flow boost but, under the legislation, should not have received it. If that's the way it pans out, that's fine, but I believe that these people are then going to get audited and we're going to have a whole lot of trouble in this area.

Mr YOUNG: Okay, we need to find out about that, Jason, because I thought it was pretty straightforward: once you submitted your BAS, you received a \$10,000 credit, minimum, on that. So I don't see how they'd be getting it without being entitled to it.

CHAIR: Let's look into it, Terry. Are you finished?

Mr YOUNG: Yes, thank you.

CHAIR: Are there any other questions?

Mr THISTLETHWAITE: Yes, just a couple of quick ones. I'm curious to know what small businesses' views are on the expediency of the ATO in dealing with some of these matters, particularly at the moment with COVID-19. I suspect that a lot of businesses are struggling and, if you are in a dispute with the tax office, you want that resolved as quickly as possible so you have a bit of certainty. So what's the experience with how quickly they're dealing with some of these issues?

Mr Phillips: The ATO did an independent survey in 2017 of people who had had tax debts and objections with the ATO. I think they surveyed about 700 people. The results of those surveys were not good for the ATO in our view. Sixty-one per cent of people said that the process was too long, too expensive and confusing.

Mr THISTLETHWAITE: Do you think that has changed during COVID-19?

Mr Phillips: I'm not aware of the Taxation Office doing any further surveys of those attitudes since then. When the ATO made a small error around the calculation of JobKeeper, we actually came out with fulsome praise of the ATO. They did a spectacular job of putting in place the JobKeeper scheme. This thing could have fallen over quite quickly, and they had extraordinarily short time lines in which to do this. I deal with a lot of accountants who specialise in small businesses. They are full of praise for the ATO on setting this up and making it smooth. In our direct dealings with the ATO on this, where we've been putting in queries and so forth on a whole range of things, they've been extremely professional and very responsive, and I can't praise them enough. But, the minute we start dealing with the audit and enforcement area of the ATO, we're dealing with the dark forces, to be dramatic about it. We haven't yet seen the ATO implementing the audit and enforcement areas, and this is, in our view and our experience, where we're going to have very major problems.

Mr THISTLETHWAITE: Thank you. Finally, you mentioned a 50-page report with some recommendations. Are you able to supply that to the committee?

Mr Phillips: I am very keen to do so, yes.

Mr THISTLETHWAITE: Okay, thank you.

Mr YOUNG: Just on that, I have talked to a lot of the business community in my area, and the feedback has been that, when they've rung the ATO during COVID, they have been over the moon with the way they've been treated. Someone has rung up and said, 'Look, I've got this tax debt.' 'No problem. You can pay it in October with no penalty.' They've been very good.

Mr Phillips: We'd agree with that. They've been absolutely outstanding.

CHAIR: I don't believe there are any other questions. Ken, one thing I want to get from you in two or three minutes is about the Taxpayer Bill of Rights in the US and the Taxpayer Advocate inside the IRS. That's also ended up in quite material reductions in the cost of collecting tax in the US. Is that right?

Mr Phillips: The figures that we've been able to put together are that, for every \$100 of tax collected in the United States, it costs 35c. In Australia, for every \$100 of tax collected, it costs 96c. So the cost of collecting tax in Australia is close to three times as high as for the IRS. We'll admit that this is not necessarily apples to apples, because there may be differences in the remit of the IRS and the ATO, so the jobs may be completely different, but it's an extraordinary difference in the cost of collection.

CHAIR: The figures that I've seen seem to indicate that that reduction—the scale benefits that the IRS has and the simpler tax system they have compared to Australia's—means that they already had a materially lower cost of collection, at around 35c to 40c per \$100, but that has halved again with the introduction of the Taxpayer Bill of Rights and the advent of the Taxpayer Advocate.

Mr Phillips: The figures we have are that in 1997 the IRS had one staff member for every 2,720 Americans. By 2019 the IRS had one staff member for every 4,150 Americans. They have had what we'd consider, since 1998, in the order of demonstrably a 50 per cent increase in their productivity. We then sought to check whether there had been a reduction in the tax take in consistent dollars. The stats that we have are that there has been no reduction; in fact, there's been a slight increase in the tax take. So there's been a 50 per cent increase in the productivity of the IRS and no reduction in the capacity to collect tax. One of the big items in that, we believe, is that the 2006 whistleblower laws in the United States have made a huge difference to the ability of the IRS to collect tax.

CHAIR: Thank you very much, Ken. Thank you for coming in today. If you've been asked to provide additional information, which you have been, could you please forward it to the secretariat by 10 July. If the committee have any further questions they will send you them in writing through the secretariat. A transcript of proceedings will be forward to you for correction in due course. I declare this hearing closed.

Committee adjourned at 11:12