



Australian Government



Australian
**Small Business and
Family Enterprise**
Ombudsman



Australian Taxation Office – enforcement of debt recovery

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Executive summary

The Australian Small Business and Family Enterprise Ombudsman (ASBFEO) has researched the issue of debt recovery action taken by the Australian Taxation Office (ATO) against small business while their Application for Review of a disputed matter was before the Administrative Appeals Tribunal (AAT). Two particular aspects considered were:

- the scale and extent of the issue for small business
- the potential impact on them.

The ASBFEO found that ATO debt recovery action happens in a sizable number of cases which are before the AAT (at least 12%) and that such action can severely impact a business' ability to prosecute its case and carry on its business. In particular, the use of garnishment (specifically enduring garnishee notices) can have a crippling impact on businesses.

This is especially true when the first knowledge of a garnishee notice is the bank not honouring payments such as wages, rent, suppliers' invoices or even loans. This has a devastating impact on a small business and the follow on effects of such actions on ability to pay, reputation and credibility is significant. There is also a real question as to whether such action is even effective since businesses will not generally have the means to emerge from this treatment to pay their ongoing tax bills, let alone carry on with their business.

Further, although our initial research was limited to historical AAT cases (particularly over the last year), the same stronger forms of ATO debt recovery actions are applied **well before** any AAT appeal has commenced, thereby impacting small businesses to a far greater degree. The ASBFEO believes from these initial findings there is further work to be done in investigating this far wider disruption of small businesses.

The ATO has a mandate to collect taxes for the purposes of Government and the ATO reports for the 2017-18 tax year that 89.5% of all tax liabilities were paid on time.¹ However, small business taxpayers face challenges different to PAYG employees or large, well-resourced corporations in meeting and disputing tax debts. Issues such as cash flow, slow payments, access to finance and working capital, technological change, workforce management and personal circumstances (such as illness) all combine to place a small business taxpayer at a severe disadvantage when pitted against one of the largest and most powerful Commonwealth Government agencies.

In respect of disputed debt before the AAT, this report details:

- debt recovery options employed by the ATO against small business
- evidence of the scale, extent and impact of the ATO's use of its enforcement powers, such as garnishee notices
- recommendations for change to improve the experience of small business taxpayers.

The ASBFEO has three key conclusions:

1. Stronger debt recovery action by the ATO kills small businesses

Any of the stronger forms of debt recovery action by the ATO (garnishees, director's penalty notices, statutory demands, and sequestration or winding-up applications) can directly cause the failure of a small business.

Whilst the ATO maintains that debt recovery action is rare for disputed debts once they are before the AAT, they still report that in 2017-18, this occurred in 17 out of 143 AAT matters.²

Where the ATO has initiated early, strong debt recovery action the resources of the small business are significantly depleted. This is a significant concern as the small business is unable to continue the process of disputing their debt.

¹ Commissioner of Taxation Annual Report 2017-18, p.29

² ATO Submission to ASBFEO April 2019, p.4

Further, an application for winding up a corporation or a sequestration order against an individual can very quickly result in the closure of a small business before the disputed matter is resolved. The liquidator or trustee in bankruptcy steps in to the shoes of the small business and can withdraw the appeal at the AAT. Given the liquidator or trustee in bankruptcy is nominated by the ATO, no such orders should be sought in respect of a matter before the AAT.

2. The ATO debt recovery action needs to be proportionate, fair and consistent

It is important that actions taken by the ATO are fair and are seen to be fair. The ATO staff should consistently adopt all internal policies and guidelines with objectivity and transparency. ATO actions should be proportionate and strong action endorsed only where absolutely necessary.

A recent review by the Inspector-General of Taxation in his joint capacity as Taxation Ombudsman (IGTO) acknowledges that although the ATO's garnishee policy, processes and practices generally seek to balance collecting debt with appropriate care, not all ATO staff on all occasions have exercised their decision making power "proportionately and appropriately".³ Although departure from policies and procedures may not be deliberate, small business cannot always rely on consistent and predictable treatment when there is a tax debt involved, and the consequences can be severe.

Immediate action to improve ATO approaches is critical since heavy-handed enforcement actions, such as a garnishee notice, effectively freezes a small business' bank accounts and can regularly mean the end of that business.

3. The ATO does not engage with small business in the same ways that it expects small business to engage

The end-to-end processes around debt recovery need to be considered using a small business lens and interactions with small businesses should be far more tailored and nuanced. For example, one of the regular complaints about ATO debt recovery calls is that the ATO telephone number shows up as 'Private Number'. A small business cannot return the call if a voicemail message is not left by the ATO. Then, when a small business taxpayer contacts the ATO to discuss debt recovery and what can be done to help resolve the issue, their call is placed in a queue for prolonged periods to be answered. The small business must then wait for the ATO staff member to familiarise themselves with filenotes and/or start their discussions again. Small businesses are notoriously time poor and the process of repeatedly dealing with the ATO is overwhelming. Anonymous calls, long wait times and repeated conversations of distressing situations do not assist a small business (nor the ATO) to resolve disputes in a timely way.



Kate Carnell AO
Australian Small Business and Family Enterprise Ombudsman

³ IGTO Review into the Australian Taxation Office's use of Garnishee Notices, March 2019

Recommendations

1. Small business must be able to seek a stay order of any ATO debt recovery action when before the AAT

In non-taxation decisions, the AAT can generally hear applications for stay orders from parties, seeking to prevent the practical implementation of a decision being disputed. However, this does not apply to taxation decisions.

Subsection 41(2) of the *Administrative Appeals Tribunal Act 1975* (AAT Act) provides that a party may request that the AAT make an order staying or otherwise affecting the operation of implementation of the decision to which the proceeding relates. However, as a result of subsection 14ZZB(1)(a) of the *Taxation Administration Act 1953*, subsection 41(2) of the AAT Act does not apply to reviewable taxation objection decisions.

As the law stands, the Commissioner usually has the power to implement a decision even where an application for review of a decision has been made to the AAT. To change that position, legislative amendment is recommended.

2. Garnishee notices must have mandated external oversight and approval

The ATO choosing to issue a garnishee notice causes immediate harm to a small business as it removes funds from the taxpayer's bank account, limiting their ability to pay wages, suppliers, rent and other operating expenses and catapulting the business into a state of technical insolvency. An 'enduring' garnishee notice, which can often last for three months, paralyses a small business by effectively freezing their bank account, making survival practically impossible without the administrative burden of changing banks and notifying customers.

The IGTO's review of the ATO's use of garnishee notices also stated:

*"Improving the ATO's garnishee case selection analytics presents an opportunity to remove from the candidate pool those taxpayers, including small businesses that are less likely to warrant enduring garnishee action to repay their tax debts."*⁴

There is clearly a real issue with the ATO application of garnishee notices to small businesses. It is important to recognise that, despite its seriousness, the ATO has the power to produce these notices without application to a court. Further, the ATO regards these notices as examples of 'firmer' action and not 'stronger action' that they view as statutory demands, actions to wind up and so forth.⁵ Should garnishee action be required, there must be mandated external oversight and approval (such as through the court system) before such an order is made.

3. Other forms of security should be used instead of garnishees

Although garnishee notices are administratively easy and a fast way for the ATO to obtain payment of a tax debt, as noted already, they are devastating to the small business. Alternative forms of security such as a Mareva injunction or caveat on property can operate to secure an asset so that it is not otherwise dealt with or dissipated, but still allows the small business to pursue normal business activities.

Funds removed by a garnishee notice are irreversible. In circumstances where the ATO has wrongly issued a notice, any funds paid by a financial institution go straight into government consolidated revenue which cannot be simply reversed.

4. Settlement deeds for matters before the AAT should be published by the AAT

There needs to be clear accountability and transparency where the ATO settles cases in an environment where a small business taxpayer is less knowledgeable and holds significantly less power. However, the ATO's model deed requires confidentiality.

⁴ IGTO op.cit. Para 2.38

⁵ See, for example, Attachment B

An anonymous contribution to our review from a stated current ATO employee commented on Deeds of Settlement entered into while the dispute is before the AAT and noted in respect of settlements:

“The imbalance of power and unconscionable conduct of the ATO leads most to relent as they don’t have the resources to continue.”

Settlement deeds creating a decision under section 42C of the AAT Act should be included as written decisions, published by the AAT, and included in the small business statistics of the ATO (including the annual report).

5. The ATO must offer the range of internal dispute resolution options and have small business acknowledgement before legal recovery action commences

Before a stronger form of debt recovery action is undertaken, the ATO must offer its range of internal review processes, including alternative dispute resolution. If resolution by these internal review processes fails then formal acknowledgement must be obtained from the small business prior to legal recovery action commencing.

The ATO currently has an in-house facilitation process for small business taxpayers but this is not consistently offered in all cases. This is a mediation process to attempt to resolve the dispute where an impartial ATO facilitator meets with the small business and the ATO case officers. We understand that the service is generally effective for less complex disputes and can be used at any stage from an audit up to and including the litigation stage. This option should be consistently offered to small business taxpayers in finalisation of audits and in the objection process.

If a tax dispute still remains, then stronger debt recovery action should generally not commence until the objection decision is made. If the ATO, in its assessment of risk regarding collection, decides to commence stronger recovery action then an Assistant Commissioner from the Review and Dispute Resolution Business line needs to authorise the action. This officer is independent from the audit or debt area of the ATO.

In cases where a small business appeals to the AAT and the ATO has a concern that funds might be dissipated, the taxpayer may alleviate ATO concerns by entering into an agreement such as a 50/50 arrangement or otherwise provide sufficient security. Further stronger action (such as bankruptcy and winding up proceedings) should not be used except in the most exceptional cases following authorisation from the highest levels within the ATO and then only with the ATO’s small business area’s input and agreement.

7. For any small business tax debt (disputed or not), adequate opportunity must be provided to pay, aligned with cash flow of the small business

The ATO has automated phone and online processes which can accept formal arrangements for repayment of a tax debt. A condition of such an arrangement is that all future obligations are lodged and paid on time. The ATO will not usually accept a proposed payment arrangement for a period of more than two years. A two year limit on a payment arrangement is arbitrary and can be detrimental to a small business taxpayer’s ability to continue to trade. Although a small business may be able to remain viable when dealing with its current tax liabilities, a reasonable repayment plan for past tax liabilities should be available.

A solution is for clear and open communication between the ATO, the small business and their professional representatives to arrange a payment plan that properly caters for the small business circumstances and is not arbitrarily restricted.

8. The ATO should continue and expand its current independent review process for small business after the pilot program finishes

A 12 month pilot commenced on 1 July 2018 to offer an independent review service to eligible small businesses disputing income tax audits. An officer from the ATO’s Review and Dispute Resolution business line conducts the review as this officer would not have been involved in the audit. The independent reviewer considers both party’s positions and prepares recommendations as to the appropriate outcome. The audit team finalises the audit in accordance with the independent reviewer’s recommendations.

The pilot currently does not include topics such as GST, superannuation, fringe benefits tax, fraud and evasion findings and interest. The pilot should be now fully implemented and expanded to ensure all small business taxation issues are considered under the independent review. This process will offer small business taxpayers with the most cost efficient method of resolving disputes with the ATO at an early stage.

Further Work

9. Expand our review to include the broader ATO debt recovery of disputed tax debts not before the AAT

While the ATO does not refute the 2017-18 statistic published on their website of 7,792 small business objections lodged with the ATO, there are no current statistics available on what percentage of these were subject to debt recovery.⁶ The disputed debt at this stage needs to be explored more fully and with a view to ensuring that transparency (including data) for these cases is present. Further, investigation of prior years would help determine whether the particular period that is the subject of the ATO data (i.e. 2017-18) is indicative of previous (and likely future) years.

The ATO's submission to this report, reproduced in Appendix A, states:

*"The only time we will recover debts in dispute is in exceptional circumstances where we see evidence of phoenixing, fraud, criminality, serious tax evasion and dissipation of assets or transfer of funds to defeat the collection of tax. These are very rare cases."*⁷

However, evidence gathered by our Office, combined with that in IGT reviews appears to contradict this.

10. Expand our review to include the availability, the timeliness and the clarity of tax law for small business

Delays in obtaining the Commissioner's view via audit position papers, private rulings and so forth has been reported to us as having a very significant impact on small business. The time taken not only produces significant taxpayer stress but can impact the viability of a business. We currently have an example of a start-up, that is subject to an ATO audit, seeking to compete in the aggregation platform market. After more than a year's delay, the position paper in this particular instance remains unsettled (even after providing extensive material to the ATO and incurring very significant tax advisory fees) and the business is unable to commence capital raising.

We are seeing examples of considerable delay in situations where there are changing technologies and business models with ATO action and inaction both having a detrimental effect on small business. Similar issues are also being reported to the ASBFEO in respect of the administration of taxation concerning research and development expenditure.

11. Investigate relevant international systems for dealing with disputed tax debt and providing legal clarity, such as the United Kingdom, United States, Ireland, Canada and New Zealand

In January 2015, the IGT published a report entitled *The Management of Tax Disputes*. Paragraph 3.83 cited examples in the United States, New Zealand and Ireland of an effective pre-assessment dispute resolution process for all taxpayers. That is, reviewing and resolving a dispute before the Notice of Assessment, which crystallises the tax debt, is issued. There will also be a natural link between work in this area and existing work being undertaken to review the Scheme for Compensation for Detriment caused by Defective Administration.

⁶ ATO Submission to ASBFEO April 2019 p.2

⁷ ATO Submission to ASBFEO April 2019 p.2

Background

On 9 April 2018, the ABC's *Four Corners* television programme aired a joint investigation with Fairfax Media into the alleged unfair treatment and heavy-handed tactics of the ATO in respect of small business taxpayers.

Several agencies were subsequently tasked with conducting inquiries and reporting on the allegations. The ASBFEO contributed to the investigation announced by the Minister for Revenue and Financial Services on 11 April 2018.

In the two weeks following the Fairfax/ABC report, we received 159 requests for assistance and submissions from small businesses and their advisors in relation to their own experiences with the ATO. We collated and analysed these cases and concluded the presence of serious system-wide issues impacting small business, including:

- 127 incidences of heavy handed practices
- 98 incidences of issues with timeframes and processes of decision making
- 29 examples of the use of garnishee notices.

The submissions from small businesses highlighted an inconsistent and undisciplined approach to debt collection by the ATO. Specific examples include:

- A small business taxpayer paid the GST liability from a Business Activity Statement late. The ATO issued a notice for an overdue tax debt and the small business immediately queried the debt and provided a copy of the receipt for the GST payment. Nevertheless, the ATO issued a garnishee notice to the small business taxpayer's bank which effectively removed all funds from the account. On the following day, the ATO issued a Statutory Demand under section 459E of the *Corporations Act* for the same debt forcing the small business to commence costly Federal Court proceedings to have the demand withdrawn.
- A small business taxpayer finalised an existing payment arrangement with the ATO. Subsequently, the small business owed further monies for PAYG and GST and superannuation. The small business applied for a payment arrangement and the ATO did not respond; neither accepting nor rejecting the small business' proposal. The ATO issued a Statutory Demand and the small business was put into liquidation and the business ceased.
- The ATO commenced an audit of a small business taxpayer in respect of a tax return ten years earlier. Before the expiration of the agreed timeframe for the small business' response to the audit findings, the ATO issued an Amended Assessment. Five days later, the ATO issued a garnishee notice in respect of the proceeds of a property sale.
- The ATO issued fines, penalties and garnishee notices in respect of two associated small businesses while the normal appeal processes and informal discussions were ongoing. The ATO finally conceded its error at the AAT and the small business taxpayers were absolved from any fault. However, the financial, operational and emotional cost to the small businesses was immeasurable.

With respect to tax disputes on appeal at the AAT, the ASBFEO received submissions from six small business taxpayers and advisors which raised concerns over the ATO's continued debt recovery actions.

ATO and the self-assessment regime

The system of 'self-assessment' means an annual income tax return or a Business Activity Statement is accepted as correct when lodged. The ATO automatically issues the Notice of Assessment (for annual income tax) unless there is deliberate intervention by the ATO to interrupt the self-assessment process. Activity statements are taken to be a Notice of Assessment on the day received by the ATO. However, small businesses under self-assessment and especially given the complexity of the tax law may be unaware of the correct application of the law and make inadvertent errors. A taxpayer may then later amend their own annual income tax return or Activity Statement when they realise they have made an error. Such "voluntary disclosures" are processed by the ATO and a Notice of Amended Assessment is issued. The ATO can generally remit (reduce or cancel) interest charges and penalties where this is fair and reasonable.

The ATO may also make enquiries, or undertake a review or audit in respect of a small business' tax affairs.

The ATO recognises that “due to the complexity of tax and superannuation law, it is inevitable that some areas of disagreement will arise”.⁸ Where a taxpayer disagrees with an ATO decision, they have the right to have that decision reviewed through the objection process.

A Notice of Amended Assessment resulting from a review or audit most likely results in an increased income tax liability. Penalties and General Interest Charges (GIC) are also imposed on the small business taxpayer’s account. In 2017-18 there were 361,107 adjustments made to taxpayers’ assessments arising from audits⁹ noting that this includes both small business and other taxpayers. Using data provided by ATO into the Inquiry into Tax Disputes (2015), we expect that approximately 20% of these adjustments would be in relation to small business taxpayers. Given the increase in the small business threshold for tax purposes from turnover levels of \$2m to \$10m, this percentage is likely to have risen significantly. This is a critical point – the pressure exerted on small business through adjustments create stress for the small business owner with options limited to either accepting the Amended Assessment or preparing a formal objection against the Notice. Either way, the increased income tax, penalties and GIC are due and payable on the date on the notice – usually 21 days.

There is, however, an opportunity for small business taxpayers to ask for an ATO facilitated mediation to achieve a possible settlement during the objection process. This process was implemented in 2015. There were only 173 small business matters settled in 2018.¹⁰ Small business taxpayers and their advisors are unlikely to be fully aware of this opportunity to resolve their dispute in the most cost efficient and timely manner (as well as the availability of the current piloted independent review mechanism which we strongly support).

ATO’s mandate for debt collection

The ATO operates as the Australian Government’s principal revenue collection agency, administering the legislation governing tax and supporting the delivery of government benefits to the community. The ATO interacts with 3.8 million small businesses including sole traders.¹¹

A Notice of Assessment, including an Amended Assessment after a review or audit, is conclusive of the correctness of the amount shown on it. If tax is payable on the Notice, it constitutes a liquidated debt due in law and payable upon expiry of the prescribed period for payment. As a general principle, the ATO expects that all debts, including those subject to dispute will be paid on time. Where tax is paid and the dispute is resolved in favour of the taxpayer, the ATO will pay interest on overpayments in respect of certain type of taxes.

The legislative framework underlying ATO policy is designed to ensure that objections, applications for review or appeals are not to be used to delay the payment of tax.¹² The Commissioner can take legal action to recover outstanding tax irrespective of whether the tax is subject to an objection, review or appeal.¹³

ATO recovery of tax debts – undisputed and disputed

There are several different methods used by the ATO to recover tax debts and 11 different classifications of debt interactions. These interactions include debt reductions, payment arrangements, negotiation, blue letters and orange letters (FAWLs), pre-legal actions and garnishee notices.

If a taxpayer cannot pay and is unable to agree the terms of a payment arrangement with the ATO, or is unwilling to engage with the ATO, the ATO will consider ‘firmer’ debt recovery actions. This may include any of the following:

- issuing a garnishee notice to a small business’ bank or a third party
- requesting financial information to assess the small business taxpayer’s ability to pay
- issuing a Directors penalty notice if a small business taxpayer is a director of a company
- issuing a statutory demand.

⁸ Commissioner of Taxation op. cit. p.36

⁹ *ibid.* Table 5.3 p. 183

¹⁰ *ibid.* Table 5.6 p. 184

¹¹ *ibid.*, p.2

¹² PS LA 2011/4 entitled *Collection and recovery of disputed debts*

¹³ *ibid.*

To recover a tax debt, the ATO may do any of the following:

- start court proceedings to obtain a judgment that a small business pays the ATO
- for individuals, initiate bankruptcy proceedings
- for companies, initiate winding up proceedings.

Where the ATO determines that the level of risk necessitates action to secure payment of a disputed debt **before** resolution of a dispute, the following options will be considered as alternatives to the initiation of legal action for recovery of the debt or possible submissions from the taxpayer to mitigate the perceived risk:

- payment of the whole debt within 14 days of a demand being issued to the taxpayer
- payment of the whole debt by instalments
- payment of 50% of the disputed debt in a lump sum with the balance being paid by instalments
- payment of 50% of the disputed debt together with the provision of acceptable security for the remaining balance
- provision of acceptable security for the whole debt
- provision of financial documents to substantiate that payment of the disputed debt would cause serious financial hardship.¹⁴

The ATO might also offer a 50/50 arrangement with taxpayers. This is an agreement whereby the taxpayer pays 50% of the disputed principal tax debt and the ATO agrees to defer collection action for recovery of the balance.¹⁵ The 50/50 arrangement usually continues through the AAT appeal stage, conditional on the ATO's continuing assessment of risk in the case. However, it should still be noted that a 50/50 arrangement is likely to place significant pressure on a small business that may also be required to liquidate assets to make the required payment.

Appeals to the Administrative Appeals Tribunal

In most cases, an applicant bears the burden of proof to establish that an assessment is excessive. A taxpayer needs to show not only that the assessment is greater than it should have been but also what the correct amount should have been.

By the time a small business taxpayer applies to the AAT for a review, in the absence of a 50/50 arrangement, the total debt will include general interest charges and penalties. This has an ongoing negative effect on small businesses with Statements of Account showing the growing debt balance being issued regularly. While the ATO is permitted under the law to continue action to recover the debt, the total owing may well now be a significantly higher value than the amount of income tax or GST in actual dispute.

The Commissioner of Taxation may agree to suspend debt recovery but the AAT cannot require the Commissioner to suspend the implementation of such a decision. A stay may only be granted by the Federal Court. This means that a small business would need to separately apply to the Federal Court to seek to ensure that a debt can be disputed before it is enforced by the ATO. However, the Federal Court gives weight to the policy priority provided by tax legislation to the recovery of revenue over the finalisation of objections and appeals. The fact that a taxpayer has a dispute is a relevant factor to be taken into account but is not itself sufficient to defer recovery action. Merits of the dispute, extreme personal hardship or abuse of the court's process may be factors that are taken into account to grant a stay.

The High Court in *Deputy Commissioner of Taxation v. Broadbeach Properties Pty Ltd* [2008] HCA 41 re-affirmed the interpretation that courts will generally not exercise their discretion to set aside a statutory demand notice because the assessments are in dispute. If a statutory demand notice is not set aside then the ATO can commence bankruptcy, winding-up and other debt recovery procedures against small businesses before a dispute is decided.

¹⁴ *ibid.*

¹⁵ *ibid.*

Further, to undertake action to seek a stay of bankruptcy or winding up proceedings is both costly and provides no certainty to the small businesses about their future. The availability of this sort of action is clearly not a fair option for small business and points to the inherent risks in seeking to dispute a decision of the ATO.

Upon commencement of bankruptcy and winding up proceedings a trustee or a liquidator, respectively, are appointed. They then become the decision-maker of the small business and we understand that this generally results in an AAT application for review being withdrawn. The small business taxpayer may have already invested significant sums in the preparation of their appeal by instructing professional representatives and all this is lost when they are replaced. Unfortunately, AAT statistics are not available to show small business applicants before the AAT being replaced by either a liquidator (for a company applicant) or a trustee in bankruptcy (for an individual applicant).

The ATO through its objection processes deals with taxpayer disputes and, using data provided by the ATO into the Inquiry into Tax Disputes (2015), showed on the figures at the time that 69% of completed objections for small business taxpayers were either allowed in full (49%) or allowed in part (20%)¹⁶. This helps support the conclusion that the ATO recognises that it is appropriate that there are small business adjusted assessments following various ATO reviews and audits. In addition, the ATO's 2018 Annual Report shows that there were 173 settled cases for small business taxpayers. In those cases, the amount of tax liabilities had been reduced by 51% in the settled amount. This evidences the importance of the ATO not launching early debt recovery when a matter is still in dispute.

The scale and extent of the issue for small business

In respect of small business disputed debt matters that are actually appealed to the AAT, the ATO reports that:

*"In 2017-18 there were 143 Small Business appeals lodged on a taxation matter in the Administrative Appeals Tribunal (AAT). There were 108 cases that were resolved in the AAT in 2017-18. The 108 cases finalised in the AAT relate to a taxpayer flagged in the ATO's system as belonging to a small business experience. Of the 108 cases finalised, 24 went to AAT decision (of which 23 were determined in the ATO's favour wholly or in part)."*¹⁷

The impact of early debt recovery on small business is, however, much broader than just those matters appealed to the AAT. The IGTO review into the ATO's use of Garnishee Notices, referred to earlier in Recommendation 1, found that in the 2016-17 financial year, the ATO issued 23,712 garnishee notices – approximately 40% less garnishee notices than the predicted 40,289.¹⁸ In 2017-18, this rose to 51,072.¹⁹ We understand that approximately two thirds of these would have been issued to small business (noting that these garnishees are across the whole system and not limited to AAT matters).

Since the IGT's Review into the ATO's management of Debt Collection in 2015, the IGTO reports that it "has continued to receive complaints about the ATO's debt recovery actions...they have consistently formed over 20% of all complaints... with the use of garnishee notices being amongst the top three topics of such complaints".²⁰

The IGT's review identified the need for targeted training content for early Intervention unit staff:

*"It is imperative that they are able to quickly develop effective skills and experience in choosing the (debt) recovery mechanism that is most appropriate to the taxpayer's circumstances."*²¹

In the March 2019 IGTO review, the number of complaints lodged with them by small business taxpayers in relation to garnishee notices from 1 July 2014 to 30 June 2018 was 135.²² After investigation, the report provides that only 44 (33%) independently assured the ATO action.

¹⁶ ATO Submission – Tax and Revenue Committee, Inquiry into Tax Disputes (4 July 2014), Table 7

¹⁷ ATO Submission to ASBFEO April 2019 p.2

¹⁸ IGTO op. cit. p.23

¹⁹ *ibid.* p. 177

²⁰ IGTO op. cit. p. 97

²¹ IGTO op. cit. Para 2.357 p. 86

²² IGTO op. cit. p.179

The majority were either resolved by the IGTO facilitating ATO resolution directly with the small businesses – 54 (40%) – or the IGTO sustained the small businesses’ concerns – 37 (27%). It was also mentioned in the report that many taxpayers would not lodge complaints with the IGTO because it would be too late after the garnishees were issued (i.e. the number of cases will be understated).

This analysis points to real deficiencies in garnishment and, given the potential consequences, is simply unfair. The tax and superannuation laws and administration system are complex and challenging for professional advisers in the field (accountants, tax agents and tax lawyers) let alone small business operators. It is important to recognise small business taxpayers, especially unrepresented ones, as more vulnerable and not subject them to arbitrary treatment. We have been made aware of situations where garnishee notices were even issued when a small business was attempting (or believed it was already in) a payment arrangement. Further, it is unacceptable that the ATO’s own documentation views garnishment as a lesser form of action compared to, say, an action to wind up a business. This evidences a failure to apply a small business lens that would recognise that an unexpected action applied, say, a week before a small business receives notification will have a disproportionate impact compared to an action to wind up that is at least able to be resisted by the business from the very start.

The ATO advises that “for the vast majority of small businesses who have a disputed debt, we will not enforce recovery of a tax debt, including even parts of the debt which are not in dispute.”²³ The ATO also advises that the only time it will recover debts in dispute is in “exceptional circumstances where we see evidence of phoenixing, fraud, criminality, serious tax evasion, dissipation of assets or transfer of funds. These are very rare cases”.²⁴

However, evidence gathered directly from the ATO combined with the IGTO report appears to show that such cases may not be considered ‘rare’ by community standards.

The impact on small business

Any form of debt recovery without a small business acknowledgement can have a devastating impact on small business. The consequences can impact other small businesses and individuals, potentially leaving employees without jobs and other suppliers unpaid. Further, given that it is the role of a small business (and any business) to collect some forms of tax such as GST, PAYG and superannuation, early debt recovery will also likely effect this collection mechanism going forward.

The IGTO garnishee review notes that:

“A garnishee notice can disrupt cash flow, cause a creditor to withdraw their credit, have reputational impact and contribute to emotional distress. The timeframe in which such impacts may be mitigated are short, particularly with the implementation of the National Payments Platform which provides for almost instantaneous payment transfers.”²⁵

A financial institution may ‘freeze’ an account for the duration of an enduring garnishee notice (generally three months) if there is insufficient cash in the account to satisfy the notice. This could cause, at the very least, administrative inconvenience in having to re-route its receivables and payments to a new bank account. Such a notice risks disproportionate financial harm to the operations of the business and its viability.

In the cases where the ATO even agrees that monies should not have been garnished from a taxpayer, the ATO is not authorised to immediately return the garnished amounts as they will have been deposited into the Government’s Consolidated Revenue Fund in satisfaction of the tax debt.

²³ ATO Submission to ASBFEO April 2019

²⁴ ATO Submission to ASBFEO April 2019

²⁵ IGTO op. cit. p.178

Concerns raised by small business in their complaints about ATO garnishee notices (and reported in the IGTO review of garnishment) include:

- the ATO should not have issued the garnishee notice at all – for example, they believe that they have no debt or have paid the debt
- the ATO should not have issued an *enduring* garnishee notice – for example, it froze the business' bank account
- the ATO should not have issued the garnishee to that source – for example, the business' trading account was garnished
- the ATO should not have issued the garnishee notice as the business owner was attempting to enter into a payment arrangement with the ATO or believes that they were already paying off the debt
- the business owner did not receive prior warning from the ATO that it would issue a garnishee notice.

On the last bullet point, it is important to note that a garnishee notice is provided electronically to the bank and applied almost instantly to an account. However, the notice to the small business taxpayer, although dispatched at the same time, is done so by physical letter delivered through the postal system and commonly from an ATO office in a different state (further adding to the delay in notification).

BRI Ferrier Adelaide reports on the consequences of being appointed Liquidator of an actively trading company by the ATO:

"Such an appointment has significant consequences for the company, its owners, employees and other creditors as the Liquidator has a limited capacity to salvage the business."

BRI Ferrier went on to provide an example, being appointed as Liquidator of a commercial electrical contractor after the ATO issued a garnishee notice to the company's seven major clients. The garnishee notice required the clients to withhold and remit to the ATO 50% of any progress claims payable to the company. The issuance of a garnishee notice enabled the clients to terminate the contracts with the effect that the company had no choice but to cease operations, resulting in the termination of 90 employees.

Robert Gottliebse, writing in The Australian on 13 February 2019, stated that:

"The ATO recently settled a substantial sum on a family who had been a beneficiary of the government's research grants. The move by the ATO destroyed the business and the family home was lost. That family received outside help to fight the ATO and win. Most tax paying small enterprises that can't raise the money lose their homes and business."

When before the AAT, the inability to obtain a stay or recovery action by the ATO further adds to the helplessness of the situation for a small business. There is a severe imbalance of power between the ATO and small business taxpayers given the disparity in terms of access to legal advice and remedies. There is no question that where the ATO commences action against a small business where a tax debt is being genuinely disputed that the consequences for the small business are dire.

Appendix A: Australian Taxation Office Submission: review on early debt recovery action on a small business disputing a debt at the AAT

The Australian Taxation Office contribution to the Australian Small Business and Family Enterprise Ombudsman's review on early debt recovery action on a small business disputing a debt at the Administrative Appeals Tribunal, April 2019.

ATO Submission

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

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

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

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

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

Small Business by the numbers

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

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

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

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

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

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

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

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

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

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

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

Responses to information requests

Scale

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

ATO Response:

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

Information Request 2: Number of ATO initiated liquidations/bankruptcies

ATO Response:

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

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

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

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

Note up

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

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

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

ATO Response:

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

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

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

Extent

Information Request 4: For matters before the AAT:

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

ATO Response:

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

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

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

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

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

Impact

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

ATO Response:

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

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

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

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

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

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

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

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

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

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

This data includes (not exhaustively):

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

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

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

ATO Response:

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

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

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

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

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

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

Dispute Assist

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

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

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

Dispute Assist can support small businesses when:

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

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

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

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

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

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

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

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

Closing

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

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

Reviewing individual cases

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

Appendices

Appendix 01- ATO Powers

Appendix 02 - Our approach is to resolve disputes

Appendix 03 - Our approach to managing debt

Appendix 01- ATO Powers

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

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

Appendix 02 - Our approach is to resolve disputes

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

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

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

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

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

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

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

The Role of the AAT

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

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

Recent initiatives to support small business

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

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

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

National Tax Clinics Trials

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

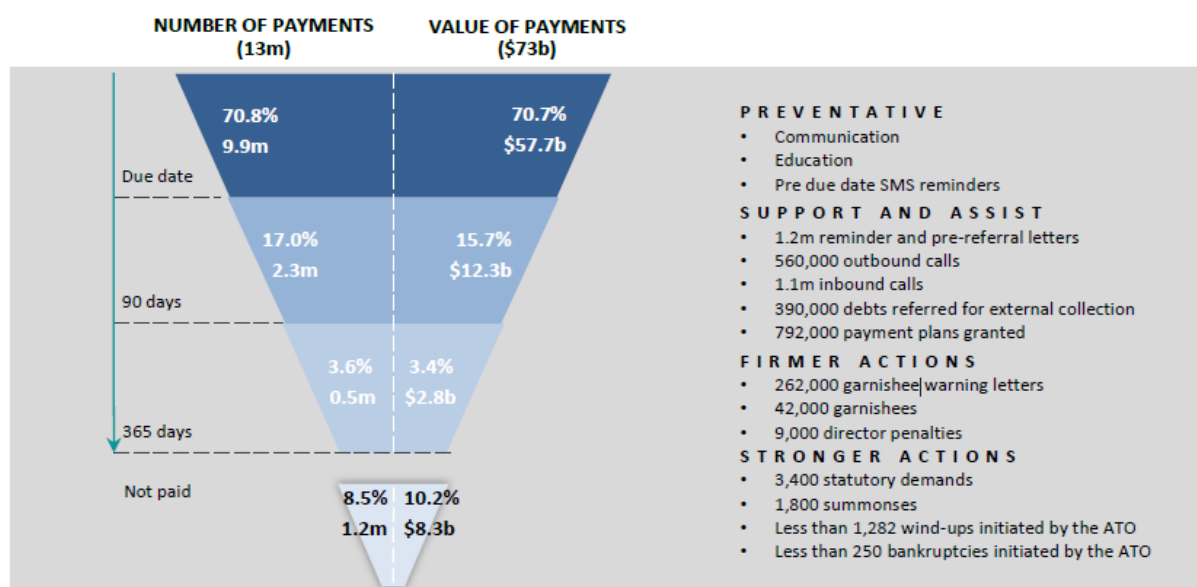
On 28 November 2018, the Government announced the National Tax Clinic Trial which will see the establishment of a further nine tax clinics in early 2019.

Appendix 03 - Our approach to managing debt

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

Figure 1. 2017-18 Small Business

2017-18 SMALL BUSINESS



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

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

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

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

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

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

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

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

Insolvency

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

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

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

Review of ATO decisions to enforce insolvency

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

The full report is included below.

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

Attachment A: 2018 Insolvency Review

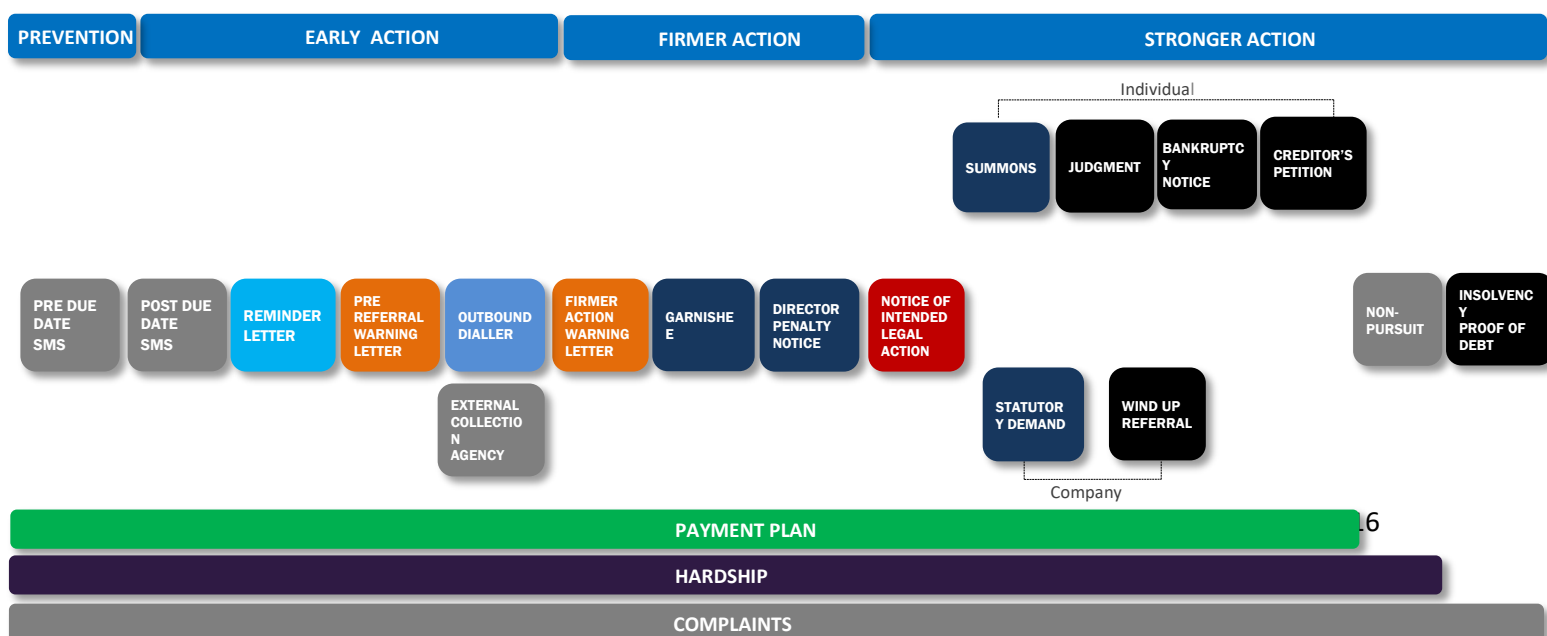


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Flow of debt cases

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

Figure 2. Flow of debt cases



Steps to ensure recovery actions are appropriate

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

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

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

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

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

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

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

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

- legal recovery
- insolvency proceedings

Garnishees – approach and safeguards

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

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

Collecting disputed debt

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

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

Freezing, seizing and selling assets

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

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

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