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Challenges of Globalising Tax Systems

**Towards Community Ownership
of the Tax System:
the Taxation Ombudsman's Perspective**



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The historical background

In the early days of taxation in England, it was the exclusive prerogative of the Monarch to make executive decisions about taxation. However, to have all decisions going up to the pre-eminent person in the land would be a very cumbersome model, one unlikely to long survive. Indeed, about 150 years ago it was recognised that

*"... as matters now stand, the Government of the country could not be carried on without the aid of an efficient body of permanent officers, occupying a position duly subordinate to that of Ministers who are directly responsible to the Crown and to Parliament, yet possessing sufficient independence, character, ability, and experience to be able to advise, and to some extent influence those who are from time to time set over them ..."*¹

Those of you who enjoyed the "Yes Minister" TV series no doubt can imagine Sir Humphrey Appleby comfortably working within this model.

In Australia, section 61 of the Constitution provides for the exercise of the executive power of the Commonwealth. It "enables the Crown to undertake all executive action which is appropriate to the position of the Commonwealth under the Constitution ..." *Barton v Commonwealth* (1974) 131 CLR 477 at 498, per Mason J. This power may be abrogated by statute; no doubt the various taxation acts abrogate the executive power of the Commonwealth to take action otherwise than under those taxation acts in relation to the specific topics they cover. Those taxation acts also confer a general power on the Commissioner of Taxation to make decisions and take the actions that are necessary to administer those acts, eg, section 8 of the *Income Tax Assessment Act 1936*, which states that the Commissioner shall have the general administration of this Act.

The Constitution in Chapter two anticipates that there will be an executive arm of Government responsible for the administration of Government policy and legislation. The tax system has always been grounded in legislation, which confers powers on the Commissioner of Taxation. The result is now a heavily legislated area. The Government has retained the right to determine tax policy, but it will choose legislation to implement that policy. The reality inevitably is that the tax system as we know it in Australia is established in legislation.

¹ Report on the Organisation of the Permanent Civil Service (1854), The Northcote-Trevelyan Report.

I understand that for many years it has been the practice for the Government of the day, when dealing with complaints about day-to-day decisions of the ATO, to assert that it is the Commissioner of Taxation who is responsible for the administration of the taxation law. In other words, freedom of the Commissioner from political interference in routine decision-making, and conversely non-accountability of the Minister in respect of routine decisions, and consequent freedom to concentrate on policy issues, would seem to have been a key value in our taxation system.

Of course, the Commissioner of Taxation has never been at large to do as he pleased. For example, he is controlled by the terms of the legislation he administers, he must report to Parliament and the Government, he is subject to audit, and his decisions may be subjected to judicial scrutiny. Other Government agencies, particularly the Treasury, contributed tax policy advice to the Government.

From the early days of taxation in Australia, it was possible for taxpayers to object to taxation assessments and, if the objection were disallowed, to seek review of the decision by a Taxation Board of Review. (In many respects, this arrangement was a pioneer model for administrative review, akin to the current Administrative Appeals Tribunal). The Boards were empowered, for the purpose of reviewing decisions, effectively to stand in the shoes of the Commissioner and exercise his powers (including discretions), and make decisions on the merits. This mix of external scrutiny for the tax office may have been adequate for the time, for it survived relatively unscathed, and apparently without undue disquiet, through much of the 20th century until the mid 1970's. However, during this time the ATO was evolving from "...a relatively small organisation with limited responsibilities to a relatively large bureaucracy with numerous social, political and economic objectives..."² The ATO continues to acquire responsibility for administering programs that are not directly related to revenue collection, such as superannuation guarantee, the baby bonus and the family tax benefit.

Increasing accountability

Administrative Law at the Federal level was revolutionised during the 1970s. First came the Administrative Appeals Tribunal³ (although this had little initial application to the ATO, because of the continued operation of the Taxation Boards of Review) and the creation of the Administrative Review Council.

Then came the *Ombudsman Act 1976*. From that time, taxpayers with a complaint had an important additional avenue to seek a remedy, the right to seek an impartial review of ATO decisions by the Commonwealth Ombudsman. Taxpayers were quick to make use of this facility:

² Report 326, *An Assessment of Tax* (November 1993) Joint Committee of Public Accounts, Commonwealth Parliament, at page 27.

³ The *Administrative Appeals Tribunal Act 1975*

In 1977-78, the first year of operation, the Ombudsman received 333 tax complaints. Numbers have fluctuated considerably over the years, reaching a peak of 3354 during 2000-2001.

The law on judicial review was reformed, with the enactment of the *Administrative Decisions (Judicial Review) Act 1977*. As a result, it became easier to seek judicial review of a wide range of decisions of the ATO.

The reform continued into the 1980s, with the enactment of the *Freedom of Information Act 1982*, helping to underwrite democratic ideals by creating rights of access to information and documents, and helping to prevent improper practice and corruption.

The Taxation Boards of Review were subsumed into the Administrative Appeals Tribunal in 1986, bringing to bear the greater capacity and resources of that Tribunal (including Presidential members) on review of decisions on objections to taxation assessments.

No doubt picking up on the mood of the times the ATO, apparently largely on its own initiative, began to consult more widely with the community. This included establishment in 1985 of National and State Taxation Liaison Groups (with representation from professional associations and the Treasury) and the Commissioner's Advisory Panel (CAP) from 1989 (including various business and community associations).⁴ The ATO also established better internal complaint handling mechanisms, responding to an increasingly educated public, more conscious of their rights, including the right to complain.

One particular example of the ATO becoming more involved with the community was its sponsorship of the development of ATAX here at the University of New South Wales (from around 1990). This initiative would have assisted the growth of external centres of excellence in taxation, and independent study, comment, and dialogue on taxation issues. This series of conferences is perhaps but one example of that process in operation.

⁴ Report 326, *An Assessment of Tax* (November 1993), Joint Committee of Public Accounts, Commonwealth Parliament.

More recent developments

(a) Parliamentary scrutiny

An interesting feature of the last decade or so has been the influence of the Federal Parliamentary committee system. The deliberations of committees can include the taking of evidence from the public as well as from tax officers and other public officials, such as the Ombudsman. Importantly, there can be input from the Opposition, minor parties and independents, so the reports do not necessarily represent Government policy, and can reflect a much wider community influence.

I have already referred to the November 1993 report of the **Joint Committee of Public Accounts**. This document made 148 recommendations that covered a wide range of tax administrative issues. Among them were recommendations to enhance the independence of the Commissioner of Taxation by requiring the tabling of any directions given by the responsible Minister to the Commissioner (recommendations 6 to 9). Other recommendations included formalising the role of Liaison Committees, facilitation of access of the public to private and public rulings and the establishment of a Taxpayers' Charter, a Commonwealth Taxation Ombudsman and a Small Taxation Claims Tribunal. Many of the recommendations seem directed at providing greater transparency, scrutiny and accountability for ATO operations. Not all of them were adopted.

More recently, problems have arisen due to the participation of many thousands of taxpayers in mass-marketed schemes. When the ATO acted to disallow tax advantages sought via the schemes, many of the taxpayers were unable or unwilling to pay the relevant tax or the accruing general interest charge. The Taxation Ombudsman investigated two of the arrangements, Budplan and Main Camp, and reports were duly published⁵. Yet another report dealt with film schemes. In the Main Camp report, the Taxation Ombudsman expressed the view that the ATO should "...bear some responsibility for the delays which have contributed to large interest bills..." It was recommended that all interest prior to 1 January 1998 be remitted, this being the date when the ATO made known its views on the particular arrangement under examination. Implicit in that recommendation is the notion that delay by the ATO in making known its views contributed to difficulties that taxpayers had in making payment of any tax properly due.

The problem then came under examination by the **Senate Economics References Committee (SERC)**. The recommendations of that Committee, and the subsequent settlement offer by the Commissioner of Taxation, went further than the Taxation Ombudsman had been prepared to recommend. Eligible investors who were prepared to settle were granted nil penalties, nil interest, and conditional two years interest-free debt repayment. As I am sure

⁵ *The ATO and Budplan* (June 1999) and *The ATO and Main Camp* (January 2001), Reports under section 35A of the *Ombudsman Act 1976*.

you will appreciate, this is a much better deal than ordinary compliant taxpayers could expect to receive should they be unable to pay tax by the due date.

Another Parliamentary Committee, the **Senate Standing Committee for the Scrutiny of Bills**, in its report *Entry and Search Provisions in Commonwealth Legislation* (6 April 2000), recommended that the Ombudsman should undertake a regular, random "sample audit" of the exercise by the ATO of its entry and search powers to ensure that those powers have been exercised appropriately. The ATO has more intrusive powers than almost any other government agency. The Taxation Ombudsman is undertaking those audits.

(b) The information and communication revolution

We hear a lot about the effect of Globalisation and the increasing power of the people to access information and new ideas, shift funds, and co-ordinate tax planning across jurisdictions. There is certainly clear evidence of this in the cases we see, although we are not well placed to gauge the full extent of this development.

Conversely, as will be seen from the foregoing discussion, there has been increasing pressure on the tax administration to disseminate quickly its views, provide electronic access to rulings, policies and practice statements, and provide early warnings to taxpayers. I have to say that in recent years the ATO appears to have made very effective use of modern communications to disseminate information to taxpayers. (Eg ATO website re tax avoidance, the public education program mounted for GST and the new tax system, the recent ATO publication on Tax Havens and tax administration).⁶

One factor underpinning the capacity of administrators to respond quickly to new developments must be new technology, and the power to analyse vast amounts of data and extract intelligence. For example, I note recent discussion in the media about global standards for dealing with and reporting suspected money-laundering arrangements.

There is also increased capacity for people to come together via the internet, gather support and apply co-ordinated political and administrative pressure. This capacity to establish and maintain contact is well illustrated by the remarkable phenomenon of mass-marketed schemes, already referred to. Here, a group of people some of whom, on one view, unambiguously set out to avoid tax⁷ were able to win concessions that would not have been achievable if they had not acted concertedly.

As an election approaches, we may again see media reports of pressure being applied to extend those concessions to participants in other tax

⁶ Tax havens and tax administration, (2004) ATO

⁷ Mackenzie J., *Borg & others v Northern Rivers Finance Pty Ltd* (2003), Supreme Court of Queensland, commenting on "a conjunction of eager sellers and eager purchasers".

avoidance arrangements. Also, the **Inspector-General of Taxation** has been asked by the Government to examine the consistency and appropriateness of ATO practices concerning remission of the general interest charge for groups in dispute with the ATO, including participants in employee benefit and other similar arrangements.⁸

(c) Official watch dogs & recent administrative changes

The **Inspector-General of Taxation** is an independent office created by the *Inspector-General of Taxation Act 2003*. The key function of the Inspector-General is to review systemic tax administration issues and to report to the Government with recommendations for improving tax administration. The sole focus for the Inspector-General is on tax systems rather than individual taxpayer matters since the Taxation Ombudsman deals with individual taxpayer disputes. The Inspector-General does not have the power to give directions or make recommendations to the Commissioner of Taxation. The review of the general interest charge, mentioned above, is a clear example of the role that the Inspector-General will perform.

Another recent creation is the **Board of Taxation**. The Board is a non-statutory body established to advise the Government on the development and implementation of taxation legislation and the ongoing operation of the tax system. A key objective of the Board is to ensure that there is full and effective community consultation in the design and implementation of tax legislation. This function includes monitoring and advising on the consultative and educative processes for the development of tax law.

The Board is also tasked with advising the Government on improving the general integrity and functioning of the taxation system and commissioning research and other studies on tax matters approved or referred to it by the Treasurer.

On 24 November 2003, the Treasurer announced the Government's decision to review the self-assessment system. This review was undertaken by the **Department of the Treasury**, and again involves extensive public consultation. A discussion paper was released in March 2004. That Department is also now responsible for the development of legislation to implement Government decisions on taxation, a function previously performed by the ATO.

(d) The role of the Ombudsman

At this stage, you may be wondering what role remains for the **Ombudsman**, first to be created among the independent watchdogs. It has to be

⁸ Media release dated 21 November 2003 by the Minister for Revenue and Assistant Treasurer, Senator the Hon. Helen Coonan,

acknowledged that there is some potential for overlap and confusion. For example, the Taxation Ombudsman currently has many complaints that raise issues related to groups of taxpayers and the general interest charge (the subject of review by the Inspector-General of Taxation), others that raise self-assessment issues (the Treasury review). One partial answer is that the Taxation Ombudsman will be working co-operatively with the newer players and will contribute our views and any insights gained from our cases. However, I should take this opportunity to reiterate the distinctive role that the Ombudsman plays in the taxation system.

The Taxation Ombudsman continues to be the only agency external to the ATO that can handle individual complaints about tax administration and resolve individual disputes. Hence, the obvious proposition is that the Taxation Ombudsman will focus primarily on individual complaints leaving the Inspector-General to conduct reviews of systemic issues.

The Ombudsman's Tax Team approaches the work of investigating and resolving complaints about tax administration from the perspective of administrative law rather than as tax law specialists. This statement should not be seen as discounting our knowledge of tax law. Rather our focus is on examining tax administration issues through the perspective of the Ombudsman Act.

Investigations by the Taxation Ombudsman are guided by the criteria spelt out in the Ombudsman Act. Our principal concern is whether an action of the ATO was contrary to law, unreasonable, unjust, oppressive, improperly discriminatory or based on a mistake of law or fact. The Taxation Ombudsman can also examine whether a legislative provision applied by the ATO, or an administrative practice followed by it, was unreasonable, unjust, oppressive or improperly discriminatory. The Taxation Ombudsman is limited to making a recommendation as to appropriate corrective action.

In working with the ATO, the Taxation Ombudsman has the advantage of his investigative experience in administrative matters over the breadth of the Federal bureaucracy, and indeed, the advantage of the corporate knowledge held in an office that has existed for over 26 years.

It is to be noted, however, that the Taxation Ombudsman's power to conduct own motion investigations remains. Again, clearly, there is some potential for overlap here. However, by appropriate liaison between agencies each will be able to complement the work of the other and cooperate closely and consistently with our respective legislation.

We envisage that we would do fewer ATO-specific own motion investigations in future. These investigations would seem to fall more logically in the Inspector-General of Taxation's area of responsibility. However, the Ombudsman often undertakes own motion investigations into matters of more general administration such as FOI, record keeping, compensation and oral

advice that cover many agencies. The ATO is a significant part of the federal bureaucracy and as such would naturally be included in such studies.

The establishment of the Inspector-General of Taxation has allowed the Taxation Ombudsman to refocus on achieving systemic remedies that arise from investigation of individual complaints. Some individual complaints indicate the presence of broader problems that can be redressed by the relatively efficient and informal processes of an Ombudsman inquiry.

This sort of approach would keep the Taxation Ombudsman's main focus on individual complaints and systemic remedies.

The Ombudsman provides an independent and informal avenue for taxpayers to raise their individual concerns. The Taxation Ombudsman follows a practical approach to complaint handling – identifying issues, setting the complaint on the path to resolution, and explaining the process to the taxpayer in a clear and open way. This serves the interests both of the individual taxpayer and of the tax system generally. The objective of our office, to achieve practical solutions to tax problems, remains vitally important.

International Comparisons

The facility for a citizen to be able to complain about taxation decisions to an official with an Ombudsman type function is by no means unique to Australia.

In the United Kingdom, the Ombudsman is an officer of the House of Commons, appointed by the Queen, and is able to consider a wide range of complaints (including those related to access to official information). Since 1993, there has also been the Adjudicator,⁹ specifically to investigate complaints about the way the Inland Revenue and the Valuation Office Agency handle taxpayers' affairs.

South Africa has a Service Monitoring Office to enable taxpayers to lodge complaints about the Revenue Service.¹⁰

New Zealand has interesting parallels with Australia. An Ombudsmen's office was established in 1962. The 1982 Official Information Act enables access to official information held by a Government agency, including the Inland Revenue Department. This Act also enables requesters to seek and obtain reasons for decisions. The New Zealand Government has indicated that it is committed to a generic tax policy process, a key feature of which is public consultation wherever practicable prior to the decision to proceed. Otherwise, there is to be consultation about the shape of the changes, after an announcement of the policy change.

⁹ The Adjudicator is Dame Barbara Mills DBE QC.

¹⁰ The Chief Executive Officer of the South African Revenue Service (SARS) Service Monitoring Office is Prof. Lynette Olivier.

In the USA, disquiet about the functioning of the Internal Revenue Service (IRS) led to the enactment of the *Internal Revenue Service Restructuring and Reform Act 1998*. The Service was required by that statute to place a greater emphasis on servicing the public and meeting taxpayer needs. The Act considerably strengthened the office of the National Taxpayer Advocate¹¹ and defined it as an independent organisation, but within the IRS. The Advocate has some 2200 employees, or about 2 percent of IRS staff.

One of the functions of the Advocate is to assist taxpayers in resolving their problems with the IRS, called the case advocacy function. The statute also authorises the Advocate to identify and propose both administrative and legislative recommendations that will mitigate taxpayer problems. Given that Australia has a Taxpayers' Charter, it is interesting to read the USA Taxpayer Advocate calling in her 2003 paper for the tax system to "...respect taxpayer rights, broadly defined to include both access and customer service. Customer service must rise to the level of a taxpayer right..."¹² Her rhetorical questions would seem to be universal: "... what about...the right to courteous treatment, prompt and accurate answers, willingness to listen and keep an open mind, helpfulness, and the technical ability of the tax administrator? Is it too much to ask of the tax administrator that he [or she] will occasionally put himself [or herself] in the shoes of the taxpayer and think about what the taxpayer is experiencing as the tax system plows on..."¹³

One of the main themes of the Advocate's report to Congress for the year ended 31 December 2003 is the need to achieve proper balance between IRS enforcement activity on one hand and customer service and taxpayer rights on the other.

*...Clearly, the IRS needs to maintain an active and vigorous presence in enforcing this country's tax laws. But these enforcement initiatives must be balanced with an equally vigorous protection of taxpayer rights, including the delivery of outstanding service...*¹⁴

Again, we daily face problems arising from this very same balancing trick.

The USA also has an IRS Oversight Board and a Treasury Inspector General for Tax Administration.

Conclusion

In the TV series, Sir Humphrey generally managed to keep the Minister on a very tight rein, and did not lightly suffer any meddling in his administration.

¹¹ The National Taxpayer Advocate is Ms Nina E. Olson.

¹² "Taxpayer Rights, Customer Service, and Compliance: A Three-Legged Stool", Nina E. Olson, Kansas Law Review 2003 Symposium.

¹³ Nina E. Olson, *op cit*, p. 4.

¹⁴ National Taxpayer Advocate, 2003 Annual Report to Congress, 31 December 2003.

Clearly, Sir Humphrey would not have made a good tax commissioner under modern conditions.

Intuitively, given the pervasive impact of taxation legislation, it seems appropriate that there be wide community input and acceptance of responsibility for design and management of the tax system.

Existence of multifaceted arrangements for consultation and review does present some problems for taxpayers and their professional advisers. When a remedy is needed, what is the most appropriate course to pursue: complaint to the ATO, complaint to a Member of Parliament or the Government, objection to an assessment and subsequent review or litigation, judicial review, complaint to the Ombudsman, or seek to involve the Inspector-General or the Board of Taxation? Or press all the buttons at once?

The answer depends largely on the nature of the problem. Is the issue one of interpretation of the law, does it raise a general systemic issue or affect large numbers of taxpayers, is a change in government policy required, or is the decision under question perceived to be contrary to law, unreasonable, unjust, oppressive or improperly discriminatory? The course to be adopted will remain one requiring some judgment, as well as an appreciation of the roles of the various agencies that might be able to assist and is as much a challenge to the tax administrators, and those overseeing the system, as for taxpayers and their advisers.