



Law Council
OF AUSTRALIA

Business Law Section

Attn: ATO Penalty Project
Australian Taxation Office
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Via email: FeedbackATOPenalties@ato.gov.au

28 October 2016

Dear Sir/Madam

ATO CONSULTATION: PROPOSED CHANGES TO PENALTIES FOR SMALL BUSINESS AND INDIVIDUALS

The Taxation Committee of the Business Law Section of the Law Council of Australia (**the Committee**) welcomes the opportunity to provide comments and submissions in response to the consultation paper outlining the ATO initiative concerning proposed changes to penalties for small business and individuals.

Broadly, the Committee believes the proposed changes are positive and that the benefits to those taxpayers affected by the changes, in particular the cost and time savings associated with dealing with such penalties, will be well received. Importantly, the approach of the ATO with respect to such penalties represents a good opportunity for the tax system to remain engaged with those taxpayers affected and to educate them in a non-threatening manner. Clearly however the proposed changes need to be carefully considered in terms of the fairness of the tax system as a whole.

Following consultation with members, the Committee has set out below the aspects of the proposed “one chance” regime that we believe require further consideration. Some of these issues were discussed at the consultation sessions that have already been held and some reflect on the questions that were raised in the ATO consultation paper issued in September 2016 (the **Consultation Paper**). The nature of the Committee’s submissions is conceptual rather than mechanical.

Unintended consequences

- It should be made more explicit that this proposed new concession is in addition to the general discretion held by the Commissioner to remit penalties, and that the one chance rule should not in any way limit the operation or application of that general discretion. It is of critical importance that any decision on the merits of the remission of a subsequent penalty (following an earlier application of the one

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chance rule) should not to be unduly influenced by the fact that a one chance has already been applied. That is, taxpayers should be in no worse position vis-à-vis subsequent penalties for having used their one chance.

- It is proposed that the one chance applies only to failure to take reasonable care penalties (25%), and not recklessness (50%). Our concern is that this threshold may unduly influence how ATO officers approach the initial application of a penalty, and may cause them to make penalty decisions that cannot be sustained from the available facts and evidence. It is the extent or degree to which the conduct of the taxpayer falls below that required of a reasonable person that underscores a finding of recklessness. The Committee would not want to see a “spike” in recklessness penalties being imposed as a result of the introduction of the new measure. The concern is not hypothetical and has parallels with other experiences. Committee members have observed in the past inconsistent ATO positions accepting a taxpayer was not exposed to penalty in some years and yet had engaged in fraud or evasion in others in respect of the same issue covering multiple years where the fraud or evasion finding was necessary to allow amendment of assessments.
- The Inspector-General of Taxation has conducted a review into the ATO’s administration of penalties, with the report to the Assistant Treasurer being released in February 2014. One of the issues noted in that report was the call for better guidance from the ATO around a number of specific areas, including circumstances where behaviour that falls significantly short of the standard of care amounts to recklessness¹. The Committee believes that the proposed changes provide a good opportunity for the ATO to revisit their guidance and provide for more certainty because, as noted by the Inspector-General, voluntary compliance is engendered where taxpayers can easily identify and clearly understand what behaviours are expected of them, especially in circumstances involving finely balanced issues².

Scoping issues

- The prevailing view amongst members was that there should be a separate “one chance” for late lodgement and for failure to take reasonable care. Broadly speaking, and as noted during the consultation sessions, these penalties operate in a different way under the *Taxation Administration Act 1953* and are directed at different behaviours. Accordingly the Committee believes that the design of the concession needs to be tailored to suit each penalty. The Committee is broadly of the view that being granted your one chance for late lodgement of a business activity statement should not take away access to your one chance for a failure to take reasonable care with respect to a technical issue in your income tax return.
- The proposed changes should not be restricted to just GST and income tax penalties. There does not seem to be any policy reason why the scope of the one chance should not be extended to other taxes and filing requirements, such as fringe benefits tax.

¹ Paragraph 5.34, “*Review into the Australian Taxation Office’s administration of penalties - A report to the Assistant Treasurer*”, Inspector-General of Taxation, February 2014.

² *ibid*, paragraph 5.35.

- The concession should be available to small businesses which operate through entities other than companies, for example partnerships and trusts. Further consideration will need to be given as to how the concession would operate in circumstances where a trust was involved. That is, is the one chance applied at the trustee level or at the level of the beneficiary? The meaning of small business, and the relevant thresholds, for the purposes of accessing this concession also needs careful consideration.
- There does not seem to be any policy reason to limit the concessions to individual taxpayers in certain categories based on whether or not they are considered to be high wealth individuals (or some other similar metric). Whilst high-wealth individuals may have access to better advice, this will not necessarily be the case. The objectives of the proposed changes and the perceived benefits, as set out in the consultation paper, remain the same regardless of the wealth of the individual taxpayer.
- It is unclear whether the concession would be extended to non-resident individuals, but there is no obvious policy reason why they should be excluded.

Other points

- Given some of the administrative complexity in designing a system that will work, particularly with respect to the failure to lodge components of the proposed changes, a staged roll-out should be considered.
- The Committee's view is that the one chance for failure to take reasonable care should be available for, and should apply to, all lodgements infected by the same error (including prior periods). Allowing taxpayers or ATO officers the ability to effectively choose the one error that gets the concession would add to complexity and potentially lead to unfair outcomes.
- Certainty is required around the "reset" rule however the Committee does not have a view as to what the appropriate period for a reset should be. Consistent with the Committee's view that penalties for failure to lodge and for failure to take reasonable care should be dealt with separately and should each attract their own one chance, the reset for each of those penalties should not necessarily be the same.
- The interaction of the once chance rule for the failure to take reasonable care penalty and the reasonably arguable position penalty should be carefully considered and further guidance provided outlining the ATO's approach to this issue. The Committee notes taxpayers and many tax agents do not fully understand the distinction between not having a reasonably arguable position and not taking reasonable care.

The Committee would be happy to provide further assistance, or discuss any of the above proposals, if that would assist. In the first instance, please contact the Committee Chair, Adrian Varrasso, on (03) 8608 2483 or via email: adrian.varrasso@minterellison.com.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Teresa Dyson', written in a cursive style.

Teresa Dyson, Chair
Business Law Section