

Holding the Tax Commissioner to Account

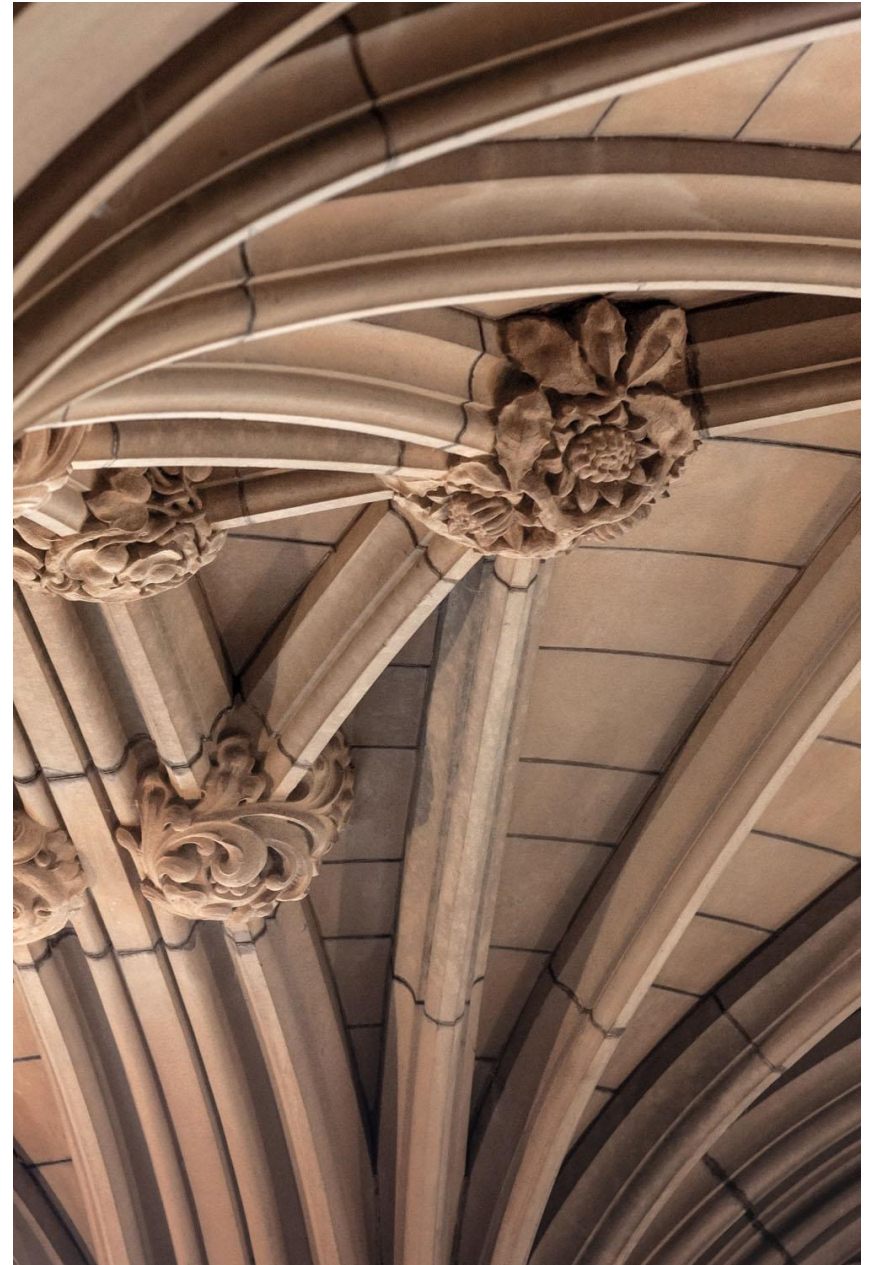
Mechanisms for external
review of decisions and actions
of the Revenue: Taxpayers and
specific decisions

Presented by

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Extensive powers are granted to the Commissioner of Taxation

Therefore the need for effective accountability mechanisms

- Powers of the Commissioner include the general power of administration as well as many specific powers
 - For example the power to assess (determine the tax-related liability) and then collect the tax debt due (extensive debt collection powers); access to premises to obtain information; requiring persons to attend and give evidence; information reporting; lodgment obligations; assessment of penalties; etc
- The level of interaction between the public and the administrator: both broad and potentially deep
- Parliamentary oversight
- Judicial oversight

External Oversight of the Commissioner and the ATO

Systemic Oversight

- Parliamentary oversight by way of Committees
 - Senate Estimates
 - House Standing Committee on Tax and Revenue
- Inspector-General of Taxation
 - Reviews of systemic issues in tax administration
- Australian National Audit Office
 - Performance and financial statement audits

Specific Decisions/Actions

- Complaints mechanisms
 - Internal to the ATO
 - External to the Inspector-General of Taxation (previously the Tax Ombudsman)
- Merits review: is the taxation decision correct?
- Judicial review: was the taxation decision correctly made?

External review of specific decisions and actions

2 potential concerns: How the power is exercised and whether the outcome (ie the tax assessed) is correct

- Merits Review: is the taxation decision correct and preferable? Goes to substantive liability
 - Allows reconsideration of the decision or issues by a Tribunal or Court
 - The right of review and appeal must be provided in law – not all decisions are reviewable
- Judicial Review: was the decision made lawfully? Goes to scope of power and process used
 - Constitutional and statutory rights to seek review by a Court
 - Is it a valid exercise of the power granted?

The importance of external accountability mechanisms

Drawing on the work of Professor Richard Mulgan, *Holding Power to Account* (2003)

- “Because the government has extensive coercive powers which can adversely affect the interests of its citizens, citizens need to be able to hold the government to account for the manner in which it uses these powers against them.”
- Linked to fundamental principles of democracy and the rule of law
- Judicial oversight and the principles of administrative law: 3 main requirements that government action should possess to be legally valid
 - That the Commissioner/ATO has acted within the authority legally granted by Parliament (not *ultra vires*)
 - That decisions have been made fairly and in accordance with due process (natural justice)
 - That decisions are not clearly unreasonable

The issue for this seminar...

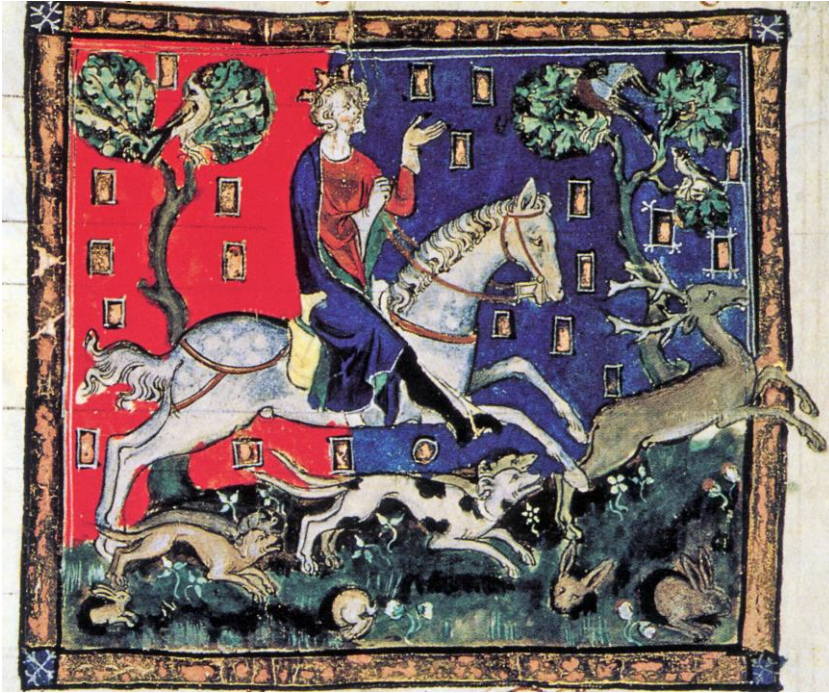
How do the merits review and judicial review mechanisms operate in the tax context and do they provide an accountability system that adequately protects the rights of taxpayers?

Merits review and challenging the substance of tax decisions

Outline of this section

- Merits review of tax decisions: deep historical roots and the link to civil liberties
- The importance of merits review under Australian law
- Overview of the merits review mechanism
 - Legal framework under the *Taxation Administration Act*

A short history of merits review: The power of taxation



King John of England, 1167-1216

Image from Wikimedia Commons

- Magna Carta (1215)
 - Limitations on taxation and feudal payments to the Crown
- Petition of Right (1628)
 - No taxes without the consent of Parliament
- Bill of Rights (1689)
 - Levying of taxes without the grant of Parliament is illegal
- Effectively, taxes can only be levied with the consent of taxpayers (provided by way of Parliament)

A developing system of review in early tax laws

- 1692 Land Tax Act
 - Power to appeal assessment if aggrieved
- 1747 Window Duties Act
 - Further development of admin system and appeals
- 1799 first English income tax
- 1803 Taxes Management Act
 - Modern features of merits review can be recognised
- 1866 first attempt to have income tax in Australian colonies – Tasmania
- 1915 Commonwealth income tax
 - CTBR then AAT in 1986



Image from Wellcome Images, UK

A right to merits review in Australia

A constitutional requirement: A tax must not be incontestable

- Dixon CJ in *Deputy Federal Commissioner of Taxation v Brown* [1958] HCA 2; (1958) 100 CLR 32:

‘Although there is no judicial decision to that effect, it has, I think, been generally assumed that under the Constitution liability for tax cannot be imposed upon the subject without leaving open to him some judicial process by which he may show that in truth he was not taxable or not taxable in the sum assessed, that is to say that an administrative assessment could not be made absolutely conclusive upon him if no recourse to the judicial power were allowed.’

- Cited with approval by the majority and Brennan J in *MacCormick v Federal Commissioner of Taxation* [1984] HCA 20; (1984) 158 CLR 622

The process that meets this requirement today: Part IVC of the *Taxation Administration Act 1953 (Cth)*

This process must be provided for in the legislation – no common law right to merits review

- Steps in the objection/appeals process (debt collection can proceed)
 1. Taxpayer objects against the assessment/decision, stating the grounds in full and in detail (time limits apply)
 2. Commissioner decides whether to allow or disallow the objection: the ‘objection decision’ (effectively a compulsory internal review)
 3. If dissatisfied with the objection decision, the taxpayer can apply to the Administrative Appeals Tribunal for a review of the decision [or appeal directly to the Federal Court]
 - The taxpayer has the burden of proving that the decision was incorrect and what the correct decision should have been
 4. If dissatisfied with the Tribunal decision, either party can appeal to the Federal Court on a question of law [and further appeals available to the Full Federal Court and, with leave, to the High Court]

Parallel oversight mechanism: Judicial review and challenging the legality or lawfulness of a taxation decision

Outline of this section

- Judicial review as a more recently recognised right
 - The ‘new’ administrative law since the 1970s
- Judicial review in the tax context
 - The phenomenon of ‘tax exceptionalism’
 - The narrowing of available grounds of judicial review under Australian law – is this problematic?

Constitutional right to judicial review

Explicitly recognised by the High Court as an entrenched right in 2003

- Section 75(v) of the *Constitution* grants the High Court original jurisdiction to hear an application for a writ of mandamus or prohibition or for an injunction against an officer of the Commonwealth
 - this jurisdiction is extended to the Federal Court by section 39B of the *Judiciary Act 1903* (Cth)
- *Plaintiff S157/2002 v Commonwealth* [2003] HCA 2; (2003) 211 CLR 476
 - ‘the jurisdiction of this court to grant relief under s 75(v) of the Constitution cannot be removed by or under a law made by Parliament’
 - So-called privative or ouster clauses in legislation cannot remove this right
- Statutory codification of judicial review in the *Administrative Decisions (Judicial Review) Act 1977* (Cth) and rights to reasons for decision

The phenomenon of 'tax exceptionalism' in administrative law

Coined by Prof Kristin Hickman, Univ of Minnesota Law School

- Where principles of administrative law/judicial review are applied in a distinct manner in the tax context
- Prof Hickman has shown evidence of this phenomenon in the US context
 - Similar system of merits review of tax deficiency notices in the US Tax Courts and judicial review by way of application of the Administrative Procedure Act to Treasury regulations
- Stephen Daly has undertaken a similar study from the UK perspective
 - Deferral to the wide managerial discretion of HMRC
 - Like the ATO in Australia, HMRC is obliged to collect the correct amount of tax due but also has a duty to properly manage public resources

Is there evidence of tax exceptionalism in Australia?

How do the review mechanisms work together?

- Judicial review guaranteed by the Constitution
 - ADJR Act excludes from its scope decisions making or forming the process of making assessments of tax (Sch 1)
 - See, eg, *Hacon v FCT* [2017] FCA 659 re application for private ruling
 - But this exclusion does not limit the jurisdiction of the Federal Court under s 39B of the *Judiciary Act*
- Merits review provided under Part IVC
- Potential to overlap so need rules to allocate jurisdiction
 - Do the rules simply allocate jurisdiction across these 2 mechanisms or is there effectively an ousting of jurisdiction?

Testing the right to judicial review in the tax context: The *Futuris* decision (2008)

What is the impact of the no invalidity clauses in the tax legislation?

- No invalidity clause: s 175 of ITAA 1936
 - ‘The validity of any assessment shall not be affected by reason that any of the provisions of this Act have not been complied with.’
- Decision of the High Court: s 175 is valid but some purported tax assessment decisions are not protected
 - A tentative or provisional assessment is not an assessment within s 175 as it does not fix a tax liability
 - Conscious maladministration of the assessment process may be said also not to produce an assessment to which s 175 applies (also called bad faith)
- The Federal Court: judicial review is now limited to only these 2 bases
- Is this a problem? Not if taxpayers have adequate review rights under Part IVC – does this approach merely allocate these issues to Part IVC?

The limits of Part IVC

Can this process test the lawfulness of the tax decision?

- The taxpayer has the burden of showing that the tax assessment is excessive or otherwise incorrect and what it should otherwise be
- Is a decision made in the purported or ‘colourable’ but invalid exercise of power still reviewable by the AAT?
 - Yes, but this is not the same as judicial review
- Can ‘excessive’ include an argument that the assessment was unlawful or invalid?
- A clear statement in the tax context: *Gashi v C of T* (2013) FFC: the subject matter of a Part IVC appeal is a valid assessment and the Court ‘does not have jurisdiction to determine if assessments are invalid’
 - So cannot raise jurisdictional error as a basis to challenge a taxation decision in Part IVC proceedings

Tension between merits and judicial review: a recent illustration

Commissioner's opinion regarding fraud or evasion & amendments of assessments

- The legislative background
 - Usual time limit for the amendment of assessments by the Commissioner: 2 or 4 years
 - If the Commissioner forms the opinion that there has been fraud or evasion, the amendment can occur at any time
 - So the opinion of fraud/evasion is a gateway to the power to make a late amendment
- How could a taxpayer challenge such an opinion/finding?
 - Merits review, as part of the objection against the assessment
 - Judicial review, that there was a flaw in the process of forming the opinion

The recent case of *Chhua v Commr of Tax* [2017] FCA 1127

- On 24 April 2013 the Commissioner issued amended assessments for income years ended 30 June 2007 – 30 June 2010 inclusive, relying on the fraud or evasion exception to the limitation period
- Txp applied for judicial review under s 39B
 - The txp asserted that the purported opinion was not an opinion at all but was merely a hypothesis based on allegations made by an informant and the audit case plan
 - The txp also asserted that the Commissioner did not take into account other relevant intelligence and did not make any enquiries about critical facts that were easily ascertainable
- Txp also objected against the assessments under Part IVC

The limits of merits review

Examined by the House of Reps Tax & Revenue Committee, Inquiry into Tax Disputes (2015)

- Steps in the objection/appeals process
 1. Taxpayer objection
 2. Commissioner's 'objection decision'
 3. Taxpayer can apply to the Tribunal for a review of the objection decision [or appeal directly to a Court]
 4. If dissatisfied with the Tribunal decision, either party can appeal to the Court [and further appeals available]
- Key point: at step 3, the taxpayer has the burden of proving that the decision was incorrect and what the correct decision should have been
 - So the txp must prove that they were not engaged in fraud or evasion
 - At a time when they may no longer have the evidence/records (usually 5 year retention period for tax records)

The limits of judicial review

- FCA in *Chhua*: opinion of fraud/evasion was a condition precedent to the power to amend late and therefore goes to substantive liability – so can be challenged in merits review process (earlier HCA authority)
 - In a judicial review case, the High Court's decision in *Futuris* requires that the taxpayer shows bad faith or conscious maladministration – not alleged in this case
- So what becomes of grounds such as: no opinion was actually formed, irrelevant considerations were taken into account, relevant considerations were not taken into account, etc?

Other examples of 'tax exceptionalism'?

- Post-*Futuris* Full Federal Court judicial review cases where questions were raised regarding the way information upon which the assessments were based was obtained
 - The Commissioner's duty is to assess based upon the most accurate information available and this is not qualified by any requirement that the Commr is satisfied that no illegality occurred in the gathering of the information
 - *Denlay* (2011): stolen information then provided to the ATO
 - *Donoghue* (2015): legal professional privilege
 - The duty to assess 'explicitly privileges the need to have accurate assessments over other private law rights'
 - *Gould* (2017): information arguably obtained in violation of treaty
- Diverted Profits Tax modified appeals regime
 - No internal or AAT review (straight to FFC) and restricted evidence

In conclusion...

- Revenue authorities need strong powers to be able to administer the complex tax systems of today and to ensure that the legally correct amount of tax is paid (assessment and collection)
- Robust external accountability mechanisms are necessary to ensure that taxpayers' rights are protected
 - The merits review system for the substantive liability
 - The judicial review system for fairness and to prevent abuses of power
 - Recent legal developments have arguably given rise to tax exceptionalism and eroded the right to judicial review
- Both review mechanisms are directed to particular taxpayers but are also important to maintain the integrity of the tax system for all taxpayers

Thank you.

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