REPORT TO THE MINISTER FOR FINANCE AND THE ASSISTANT TREASURER

REVIEW OF THE COMPENSATION FOR DETRIMENT CAUSED BY DEFECTIVE ADMINISTRATION SCHEME IN RELATION TO THE AUSTRALIAN TAXATION OFFICE AND SMALL BUSINESS

JUNE 2019

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Senator the Hon Mathias Cormann
Minister for Finance
Parliament House
CANBERRA

The Hon Michael Sukkar MP
Assistant Treasurer
Parliament House
CANBERRA

14 June 2019

Dear Minister and Assistant Treasurer

I am pleased to present my Report on the Review of Compensation for Detriment Caused by Defective Administration Scheme in relation to the Australian Taxation Office and small business.

The Review commenced in mid-February and has been completed as required by 14 June 2019. The Review undertook a detailed investigation into the history of the CDDA Scheme since it was established in 1995 and consulted widely in accordance with the terms of reference. Virtually all the agencies, organisations and people approached for an interview were keen to assist us. A few people came directly to the Review and a small number provided written submissions.

The Commissioner of Taxation, senior ATO and General Counsel officers were very cooperative throughout the Review. The Treasury gave the Review helpful insights and the Department of Finance provided detailed briefings and timely and competent administrative support.

All of those contributions are gratefully acknowledged.

Yours sincerely



Robert Cornall AO

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TERMS OF REFERENCE

1. The Review will examine the operation and implementation by the ATO of the Compensation for Detriment Caused by Defective Administration (CDDA) scheme as it relates to small business.

2. The Review will address perceptions that the scheme does not always adequately compensate small business taxpayers for the effect of defective administration. It will consider how independent decision-making is best achieved in relation to CDDA claims.

3. For the purposes of the Review, small business is defined as an entity, including companies, trusts, partnerships and sole traders with an annual turnover of less than $10 million per annum.

4. The Review will consider evidence from the ATO over the last five years, including:

   a. the processes used by the ATO to consider and decide on CDDA claims;

   b. claims data such as the number of claims involving small business, the number of successful claims as a proportion of total claims made and where the claims are approved, the adequacy of the compensation to the detriment suffered;

   c. how often CDDA claims are reviewed internally by the ATO and externally by the Commonwealth Ombudsman, and the outcomes of such reviews; and

   d. the cost and time impacts on small businesses which seek compensation through the CDDA process.

5. The Review will consider the consistency of how CDDA processes involving small businesses are conducted across the ATO, the handling of conflicts of interest, the timeliness of the processes and how effectively the outcomes are communicated to small businesses.

6. Findings drawn from the Review will allow for evidence based future policy making on the best mechanisms to provide small business with access to a fair, efficient, accountable and transparent system for administrative review. The Review is not a mechanism for review of previous CDDA decisions by the ATO.

7. The Review will be conducted by the Department of Finance, led by an eminent Australian and supported by a consultant. The Review will consult with small business, the ATO, the Inspector-General of Taxation (IGT), and other bodies responsible for external reviews, such as the Office of the Commonwealth Ombudsman.

8. The Review will commence in early 2019 and will be provided to the Department of Finance by mid-2019.

GLOSSARY

AAT	Administrative Appeals Tribunal
ASBFEO	Australian Small Business and Family Enterprise Ombudsman
ATO	Australian Taxation Office
BAS	Business Activity Statement
CDDA	Compensation for Detriment caused by Defective Administration
Finance	Department of Finance
General Counsel	The Office of General Counsel within the ATO Corporate business line
GST	Goods and Services Tax
IGT	Inspector-General of Taxation.
Law Design and Practice Group	The ATO's Law Design and Practice Group includes the Review and Dispute Resolution business line
Ombudsman	Commonwealth Ombudsman
PGPA Act	Public Governance Performance and Accountability Act 2013
R&D	Research and Development
Resource Management Guide	Scheme for Compensation for Detriment caused by Defective Administration Resource Management Guide No 409 issued by the Department of Finance
Scheme	The Compensation for Detriment caused by Defective Administration Scheme
Tax Act	The Taxation Administration Act 1953
Tax Office	Australian Taxation Office
Taxation Ombudsman	IGT is also referred to as the Taxation Ombudsman since 1 May 2015
The Commissioner	The Commissioner of Taxation

EXECUTIVE SUMMARY

The Compensation for Detriment Caused by Defective Administration Scheme was established in 1995 when that category of compensation was separated from the Act of Grace remedy. Cabinet agreed that Ministers were best placed (personally or through their authorised agents) to determine claims of defective administration against their department and agencies in their portfolio. They do so using executive power under section 61 of the Constitution.

Payments made under the CDDA Scheme are discretionary and the compensation is assessed against a yardstick of fairness (which was originally described as a moral obligation), not legal liability. The purpose of the Scheme is to restore the claimant to the position they would have been in had the defective administration not occurred.

The Scheme covers all Australian Government agencies[1] and it is administered in accordance with Resource Management Guide No 409 issued by the Department of Finance. The guidelines have very largely stayed the same since the Scheme commenced.

From the beginning, it was anticipated that the CDDA Scheme would be used mainly by the small number of agencies which have direct dealings with the public and that has proved to be the case. Today, those agencies include the Australian Taxation Office, the Department of Human Services (Centrelink, Medicare and Child Support programs) and the Department of Home Affairs.

The procedure under the CDDA Scheme is, first, to decide if there is defective administration and then go on to assess any directly resulting detriment and to quantify the loss. In some cases, such as a missed social security payment, the defective administration can be clear and the detriment easy to quantify. Other cases require significant judgments to be made. The guidelines are sufficiently flexible to allow narrow or more generous interpretations of the same circumstances.

This issue was brought out strongly in the Ombudsman's 1999 report, *To compensate or not to compensate?* Although that was a long time ago, the Ombudsman's contemporaneous opinion about the implementation of discretionary compensation mechanisms including the CDDA Scheme – just four years after it commenced – is still relevant today. The Ombudsman said:

> *… the compensation mechanisms … can be interpreted broadly enough to enable agencies to pay compensation in all cases where they believe it is warranted, or narrowly enough to exclude any request, depending on the agency's approach to compensation generally or in individual cases*.[2]

[1] That is, non-corporate Commonwealth entities

[2] *To compensate or not to compensate*, paragraph 10

> *… we believe agencies could provide compensation more often than they do, by adopting a more flexible, customer focused approach based on a broad interpretation of the powers available to them and by reference to standards they set themselves, for example, in their service charters.*[3]

In 2017-18, the ATO's net tax collections were almost $397 billion and its compensation payments under the CDDA Scheme totalled $409,035. Looking at the ATO big picture, an uninformed observer might assume the Scheme was of little importance but the opposite is the case. Concerns for small business and adverse perceptions of the ATO's administration of the CDDA Scheme have attracted constant attention.

Over the last two decades, the CDDA Scheme and the Tax Office have been the subject of, or included in, reviews, inquiries and reports by parliamentary committees, the Ombudsman, the Inspector-General of Taxation, the Australian National Audit Office, the Department of Finance, the Treasury, the Administrative Review Council, the media and other commentators including the Australian Small Business and Family Enterprise Ombudsman. The reviews and reports listed in Appendix 2 have consistently raised concerns about the Scheme and suggested improvements.

The adverse perceptions of the CDDA Scheme identified throughout this Report and its limited use over the last five years indicate the Scheme is not working effectively for taxpayers in their dealings with the ATO. Some of the concerns arise from the inherent limitations of the Scheme. Other concerns involve the ATO's procedures and implementation discussed in this Report.

This Review is focused on small businesses with an annual turnover of less than $10 million. The ATO provides a very useful statistical analysis of businesses in this category in *Small business by the numbers*.[4]

The statistics show that small business is a vital component of the Australian economy. Australia's 3.8 million small businesses employ around 5.2 million employees and contribute $380 billion to the Australian economy. The statistics also indicate the fragility of these small businesses and their lack of resources. Eighty-three percent of them have a turnover less than $100,000 and 78% of small businesses have no employees.

Compliance with complex tax legislation poses large challenges for small business, particularly in areas such as research and development, superannuation, goods and services tax and personal services income. The Government and the Tax Office recognise those problems and regularly introduce reforms and new initiatives to improve small business' ability to comply with their tax obligations.

Problems can also arise for many small businesses due to the length of time compliance processes can take. Time away from the business and the cost of professional assistance can have a damaging effect even though the review or audit has been conducted by ATO officers in accordance with the prescribed procedures and timelines. In those cases, there is no defective administration and no compensation under the CDDA Scheme.

[3] Executive Summary, paragraph 8

[4] See Appendix 3

Similarly, if a small business taxpayer is successful in an objection to a tax assessment, there is no reimbursement of the costs incurred as Parliament has not made any provision for such a payment in the governing legislation.

It follows that ATO compliance procedures can have a disproportionate impact on a small business and cause significant adverse financial and personal outcomes. The Review suggests the Commissioner consider the practicality of requiring ATO officers to take a small business' financial and personal capacity to respond to a review, audit or other compliance process into account as one factor in discharging their duties. If such a requirement was introduced, failure to do so could potentially form the basis for a CDDA claim.

One fact that stands out immediately on examining the ATO's CDDA claims history is how small some of the compensation payments are. This is not a criticism but a statement of fact that was as true in 2011 (when the Department of Finance conducted a government-wide survey of the Scheme) as it is today.

The small payments can come about in this way. If, for example, the ATO's late payment of money due was found to be defective administration, then the detriment is likely to be quantified as lost interest for the period of the delay. Other common small payments cover bank fees, postage, telephone costs and other directly resulting out-of-pocket expenses.

Those small amounts of compensation have led small businesses and their professional advisers to decide it is not worth applying for compensation and that the CDDA is a 'token' scheme. If a small business decides to make a claim, it may incur further costs that cannot be recovered through the CDDA Scheme and the costs may exceed any compensation received.

At the other extreme, there is no limit on the amount of compensation payable under the Scheme as long as the payment is publicly defensible and some large amounts have been paid out as compensation for defective administration.

The Review has closely examined the CDDA Scheme and the ATO's management of it and made twelve recommendations.

The first recommendation deals with the nature of executive schemes. In the ATO's case, the administration of the CDDA Scheme is vested in the Assistant Treasurer. While some Ministers in other agencies have occasionally decided CDDA claims themselves, it is more common for a Minister to specifically authorise officers to do so as the Minister's agent.

The Review understands a CDDA briefing is included in the ATO's Incoming Government Brief. However, as the Minister could be held accountable for a contentious CDDA decision, the Review considers it is good practice for an incoming Minister to issue new authorisations to their agents and be satisfied about the way the CDDA Scheme is being administered.

The Review has offered some suggestions for process refinements in the ATO's administration of the CDDA Scheme. They include:

- categorising claims as straightforward, standard or complex, significant or sensitive and adjusting its processes for each of the three categories

- separating the investigation and decision making functions and involving senior officers from other business lines as decision makers in category 2 and category 3 claims

- following more precisely defined procedural fairness processes

- taking a more liberal approach to offering and accepting requests for internal review and having different categories of claims reviewed by independent, senior officers and possibly an external reviewer in a small number of the most complex, significant or sensitive claims, and

- redrafting the ATO's standard CDDA documentation and correspondence with claimants in succinct, everyday language, noting that the current letter templates are likely to be a major factor in the perception that the ATO approach is too legalistic and claims are too narrowly interpreted.

The ATO adopts the balance of probabilities standard of proof (more than 50%) in CDDA claims. The Review considers the standard of proof required by the Resource Management Guide is the lower standard of plausibility and recommends adopting that standard in future.

Based on the comments and perceptions that came to the Review's attention, a major criticism of the Scheme as administered by the ATO is that it is not widely known or understood. The Review considers more can be done to raise small business awareness of the CDDA Scheme and recommends a comprehensive and ongoing communication program to address that issue.

The Government recently introduced a concierge service for vulnerable small business taxpayers representing themselves at the Administrative Appeals Tribunal. The concierge service is managed by the Australian Small Business and Family Enterprise Ombudsman. The Review considers a similar service could help small businesses seeking to make a CDDA compensation claim and recommends the establishment of a Small Business Compensation Assistance Service, also to be run by the ASBFEO.

The ATO established the Law Design and Practice Group in 2015 as an independent appeals body within the ATO. The Review considers that, while compensation claims are decided on a discretionary rather than a legal basis, there are some process synergies which would be achieved by co-location. Accordingly, the Review recommends the Commissioner consider moving the CDDA function from the Office of General Counsel to the Law Design and Practice Group.

Finally, the Review came back to the views put forward by the Ombudsman 20 years ago. What amounts to defective administration by the ATO has to be considered in the context of its legislation, the exercise of its statutory powers and compliance with its prescribed procedures. Detriment has to take account of the impact the ATO's administration can have on taxpayers and recognise that it can have a disproportionate and very damaging impact on small business.

The Commissioner can, within the Minister's authority, define defective administration, detriment and the application of the CDDA Scheme to suit the ATO's unique circumstances and so it addresses what the Commissioner has referred to as the ATO's 'real mistakes'.

With those factors in mind, the Review recommends the Commissioner set a strategic objective for the ATO's use of the CDDA Scheme and proposes the development of an implementation plan to achieve the ATO's goal.

While the changes proposed by the Review will come at some cost to the ATO, the following points should be taken into account. First, the proposals respond to concerns and adverse perceptions that have been raised on many occasions. Secondly, taxpayer perceptions that they are being treated fairly make an important contribution to voluntary compliance in a self-assessment tax system.

RECOMMENDATIONS

Recommendation 1: That good practice in the management of CDDA claims in the ATO would involve briefing and conferring with each new portfolio Minister with CDDA Scheme responsibility in regard to:

1.1 the Minister's primary role in relation to the Scheme and potential accountability for CDDA decisions

1.2 fresh authorisations for specific ATO officers to investigate CDDA claims and make CDDA decisions as agents of the Minister within specified limits

1.3 the Minister's instructions and guidance about the administration of the CDDA Scheme on the Minister's behalf, and

1.4 how the ATO proposes to administer and report on the Scheme in accordance with the Minister's instructions and guidance (if any) and Finance's Resource Management Guide No 409.

Recommendation 2: That the ATO further develop its procedures for handling claims for compensation in a more comprehensive CDDA Manual which includes:

2.1 categorising claims into three categories (straight forward; standard; and complex, significant or sensitive) with varying procedural requirements depending on the nature and circumstances of the claim.

2.2 separating the investigation and decision making functions for claims in categories 2 and 3.

2.3 providing the claimant with the opportunity to consider and comment on the investigator's preliminary view of claims in categories 2 and 3 before a decision is made.

2.4 taking a more liberal approach to offering, and accepting requests for, internal review of decisions in categories 2 and 3 if there appears to be a reasonable basis for it.

2.5 redrafting CDDA documentation and decision letters in more succinct, everyday language.

2.6 providing a regular report on CDDA matters direct to the Commissioner.

Recommendation 3: That the Commissioner give the ATO's CDDA practitioners guidance about the interpretation of defective administration and detriment in CDDA claims made by small business.

Recommendation 4: That, if necessary, the ATO amend its service, conduct or performance standards to support the Commissioner's guidance on the interpretation of defective administration.

Recommendation 5: That the ATO adopt plausibility as the standard of proof in CDDA claims instead of the balance of probabilities.

Recommendation 6: That the Review does not support calls for removal of confidentiality agreements from deeds of release.

Recommendation 7: That the ATO undertake a comprehensive and ongoing communication program to raise awareness about the CDDA Scheme among small businesses, tax professionals and their professional bodies and to assist other organisations and members of the public who want to know about ATO compensation.

Recommendation 8: That the Government establish a Small Business Compensation Assistance Service open to all small businesses to be administered by the Australian Small Business and Family Enterprise Ombudsman.

Recommendation 9: That the CDDA function be moved from the ATO Corporate business line to the Law Design and Practice Group.

Recommendation 10: That the Commissioner consider the practicality of including an appropriately worded requirement in the ATO's prescribed procedures specifying that a small business' financial and personal capacity to respond to a review, audit or other compliance process is a factor to be taken into account by ATO officers in discharging their duties.

Recommendation 11: That, in consultation with the Minister, the Commissioner sets a strategic objective for the ATO's use of the CDDA Scheme and vests the responsibility for developing and implementing an implementation plan to reach the ATO's goal in the Second Commissioner, Law Design and Practice.

Recommendation 12: That the implementation of these recommendations be monitored by the Second Commissioner, Law Design and Practice and annual progress reports made to the Minister and the Secretary with a thorough evaluation of outcomes in 2022-23.

SECTION 1: INTRODUCTION

The Minister for Finance and the Assistant Treasurer jointly announced the commencement of this Review of the Scheme for Compensation for Detriment Caused by Defective Administration on 25 February 2019[5].

The CDDA Scheme:

> *…is a discretionary mechanism available to non-corporate Commonwealth entities. It allows an entity to pay compensation when a person or organisation has suffered detriment as a result of the entity's defective administration, when there is no legal requirement to make a payment.*[6]

The history of the Scheme and an explanation of how it works are dealt with in Section 3.

The Review is one of several government responses prompted by an ABC program which the House of Representatives Standing Committee on Tax and Revenue has described in these terms:

> *On 9 April 2018, the provocatively titled ABC Four Corners program 'A mongrel pack of bastards' was aired. It featured a number of aggrieved small businesses who accused the ATO of unfairness, ineptness and even illegality in its actions against these taxpayers.*[7]

Those accusations were strongly contested by the Commissioner of Taxation in the media and in the ATO's Senate Estimates hearing before the Economics Legislation Committee on 30 May 2018. However, the public debate following Four Corners focused attention on the continuing need to find ways to assist and support small businesses in their dealings with the Tax Office.

In a speech delivered on 28 November 2018, the Prime Minister, the Hon Scott Morrison MP, listed the government and ATO actions taken or in prospect to help small business to deal with tax complexity and red tape. He said:

> *But I understand the concerns … of small business when it comes to dealing with the ATO. There is no denying the complexity involved and we are focused on reducing that complexity. …*
>
> *The Government will also be reviewing the avenues through which small businesses are compensated if the ATO's handling of the case causes an economic or personal loss. The review will be run out of the Department of Finance and they will report back in the new year.*[8]

[5] The Review began its work on 18 February 2019.
[6] Scheme for Compensation for Detriment Caused by Defective Administration, Department of Finance, Resource Management Guide No 409 (November 2018)
[7] Review of 2017 Annual Report of the Australian Taxation Office, published February 2019, paragraph 3.9, page 55
[8] Speech to the Australian Chamber of Commerce and Industry Annual Dinner

As a result, this Review is not a general review of the CDDA Scheme. It was commissioned for the limited purpose of considering the operation of the Scheme by the Australian Taxation Office in relation to small business entities with an annual turnover of less than $10 million. 'Entities' includes companies, trusts, partnerships and sole traders.

The Review was required to consider evidence from the ATO covering the last five years and:

> *… the consistency of how the CDDA processes involving small businesses are conducted across the ATO, the handling of conflicts of interest, the timeliness of the processes and how effectively the outcomes are communicated to small businesses.*[9]

In addition, in their joint announcement, the Ministers included:

> *The adequacy of compensation for small businesses that have suffered an economic and/or personal loss as a consequence of the ATO's actions.*

Finally, the terms of reference called on the Review to consider perceptions that the Scheme does not adequately compensate small business taxpayers for the effect of defective administration.

Details of the Review's consultations, investigations and research are set out in Section 2.

This Report had to be provided to the Department of Finance by mid-2019.

[9] Terms of reference, paragraph 5

SECTION 2: THE CONDUCT OF THE REVIEW

One of the Review's first tasks was the development of a Review Plan including Stakeholder Engagement Strategies. The plan was finalised on 24 February 2019.

The plan contained a small business consultation strategy and a government entity consultation strategy together with a list of proposed interviewees for each group.

The work to be undertaken was loosely divided into five phases of three or four weeks each spread over the time available for completion of the Review:

- phase 1 was mainly focused on: initial meetings with Department of Finance officers, the Commissioner of Taxation and Treasury officials; obtaining and reviewing material relevant to the terms of reference (including detailed briefing material from the ATO's Office of General Counsel, background information about the establishment and development of the CDDA Scheme since 1995 and a large number of previous reviews of, and commentaries on, the Scheme, its operation and shortcomings); and contacting proposed interviewees seeking an appointment for interview

- phase 2 was largely taken up with: interviews; following up on information or leads provided by interviewees; and a continuation of the research and investigations already underway

- in phase 3, the Review: completed the remaining interviews; gave initial consideration to further relevant material as it came to hand; and followed up outstanding lines of enquiry

- phase 4 included: a thorough analysis of all the information collected so far; discussion about issues with the CDDA Scheme as administered by the ATO; the development of tentative recommendations to address them; and initial drafting of this Report, and

- in phase 5, the Review: completed drafting the Report; tested its recommendations for practicality; checked the text for factual accuracy and that it met the terms of reference; undertook an appropriate procedural fairness process; and delivered the Report by 14 June 2019.

A list of agencies, organisations and persons interviewed is attached at **Appendix 1**. The Review received several written submissions which are set out in the table below.

Table 1: Written submissions

GOVERNMENT AND OTHER ORGANISATIONS
• Australian Chamber of Commerce and Industry • CPA Australia • Institute of Chartered Accountants Australia and New Zealand • The Western Australian Small Business Commissioner • Institute of Public Accountants
INDIVIDUALS
• Ms Helen Petaia • Mr Mark Freeman • Ms Joanne Hambrook • Mr Ashley Moore, Moore Lawyers • Mr Peter Barwell

The Review's principal contact in the Australian Taxation Office was with lawyers in the Office of General Counsel. They provided a great deal of material, documentation, information and assistance throughout the course of the Review. In particular, General Counsel gave the Review:

- manually identified lists of 50 successful and 50 unsuccessful small business CDDA claims processed by the Tax Office over the last five years[10]
- details of specific CDDA claims upon request
- a copy of General Counsel's CDDA Manual
- a detailed understanding of its process and procedures, and
- advice about its interaction with other Tax Office business lines.

The Department of Finance was responsible for administrative support.

The Review did not actively seek submissions but it was pleased to receive submissions from interviewees when offered. In addition, the Department of Finance hosted a Review website which contained basic information about the Review, an invitation for public submissions and contact details.

The CDDA Scheme as presently administered by the Tax Office has only paid out relatively small amounts of compensation to all claimants under the CDDA Scheme (not just small businesses) over the last five years.

[10] The two lists had to be manually identified as the ATO does not record the category of taxpayer making a CDDA claim or their annual turnover

In 2017-18, the ATO reported:

> *… we registered 171 and finalised 166 compensation claims, with 76 resulting in compensation being offered.*
>
> *The total amount of compensation payments made in 2017-18 was $409,035. The median payment was $495 and the average was $7,575.*[11]

Despite those low figures, the CDDA Scheme and the ATO's administration of it has been the subject of constant government, parliamentary, stakeholder, public and media scrutiny since 1995. A list of Key CDDA Reviews and Milestones is attached at **Appendix 2**.

[11] ATO Annual Report 2017-18, Appendix 5: Compensation Statistics, page 192

SECTION 3: THE NATURE OF THE CDDA SCHEME

The Australian Government has long acknowledged the need to pay compensation in some circumstances where it has no legal liability but government agencies must have legal authority to make such payments.

The CDDA Scheme is one of three discretionary Commonwealth schemes that may provide compensation or financial relief for claimants arising from their dealings with the Australian Taxation Office. While this Review is only concerned with CDDA claims, it important to be aware of the Act of Grace and Waiver of Debt Schemes as well.

3.1 Act of Grace and Waiver of Debt

The following statements are taken from the Department of Finance information brochure titled *Act of Grace Payments*:

> *Section 65 of the Public Governance, Performance and Accountability Act 2013 allows the Finance Minister to make payments that would not otherwise be authorised by law. The act of grace power has been delegated to officials within the Department of Finance.*
>
> *Act of grace payments are discretionary.*
>
> *They may be made by the Finance Minister or delegate when it is considered appropriate to do so because of special circumstances.*
>
> *The act of grace mechanism is generally an avenue of last resort. It is not used where there are other avenues available to provide redress.*

While 'special circumstances' are not defined, the brochure indicates they may apply where the act of an agency has caused an unintended or inequitable result to an individual or organisation; Commonwealth legislation or policy has had an unintended, anomalous, inequitable or otherwise unacceptable impact on the claimant's circumstances; or the Commonwealth intends to introduce legislation or policy covering the matter.

The following statements are taken from the Department of Finance information brochure titled *Waiver of Debt*:

> *A waiver is a special concession granted to a person or organisation that extinguishes a debt owed to the Commonwealth. This means the debt is completely forgiven and can no longer be recovered.*
>
> *Under section 63 of the PGPA Act, the Finance Minister may waive amounts owing to the Commonwealth. The waiver of debt power has been delegated to officials within the Department of Finance.*

The waiver of debt power is discretionary.

Debts may be waived where the decision maker considers recovery of the debt would be inequitable or cause ongoing financial hardship, and that other debt treatment options (such as an agency writing off the debt or deferring payment) are not appropriate. The waiver of debt mechanism is generally an avenue of last resort. It is not used when other viable avenues of redress are available.

There are two significant differences between these two schemes and the CDDA Scheme:

- act of grace payments and debt waivers are made at the discretion of the Minister for Finance or the Minister's delegates, and

- those discretionary decisions are authorised by statute.

3.2 The CDDA Scheme

Before the CDDA Scheme was established, discretionary compensation was limited to act of grace and ex-gratia payments. Claims of maladministration or defective administration were considered under the act of grace arrangements.

From December 1988, responsibility for act of grace payments was devolved from the Minister for Finance to agency heads who were appointed under the *Audit Act 1901* for a two year trial which was followed by an evaluation in 1991. The trial lasted until the CDDA scheme was established as an administrative (not legislative) scheme utilising the executive power of the Commonwealth.[12]

On 24 October 1995, the Cabinet agreed:

> *… to the establishment of a scheme for compensation for detriment caused by defective administration by an Agency, to be administered by each Minister for the Agencies under his or her control*.[13]

Cabinet submission 2207, which recommended the Cabinet's CDDA decision (and was attached to it), noted:

> *Commonwealth 'gratuitous' payments – made as a matter of choice, rather than under any statutory, contractual or other legal obligation – reflect the Government's policies and collective decisions. … The legal authority to approve payments, against available appropriations, derives from the responsible Ministers' constitutional powers.*[14]*…*
>
> *Claims for compensation that do not meet the conditions set out in the criteria would be able to be referred to Finance for consideration under the normal act of grace conditions.*[15]

[12] Constitution, section 61
[13] Cabinet Minute No 4549
[14] Submission 2207, Background, first paragraph
[15] Submission 2207, Background, paragraph 17

Paragraph 1 of Attachment G to submission 2207 contained this caution:

> *Where authority is given by a Minister to an Agency official to approve payments under this Scheme, that authority is to be conferred expressly – that is, separately from the Minister's general authorisation to incur expenditure. [This requirement is in recognition of the special and potentially sensitive nature of decisions that may be made under the Scheme, for which the Agency and its Minister may be held accountable].*

The fact that the CDDA Scheme is an executive (or administrative) scheme is important.

Agencies administering the CDDA Scheme are guided by instructions (if any) from their Minister and policy documents issued by the Department of Finance. That guidance can be changed at any time.

In *Salemi v MacKellar (No 2)*, Barwick CJ said[16]:

> *Statements of policy as a rule do not create legal obligations, though they may understandably excite human expectations as distinct from lawful expectations. … Governments are free to change policies. They are also free not to implement them.*

The basis for payment of discretionary compensation for defective administration where there is no legal liability was explained this way in Cabinet submission 2207:

> *These cases arise where the circumstances demand an equitable remedy, but are not sufficiently clear or strong enough to lead to a conclusion that the Commonwealth would be found legally liable if the matter were litigated.*[17]

More commonly, the basis for compensation was expressed as a 'moral obligation'. For example, the policy guidance in Finance Circular 2006/05 *Discretionary Compensation Mechanisms* explained that CDDA payments are approved:

> *… at the discretion of the decision maker … on the basis that there is a moral, rather than purely legal, obligation to the person or body concerned.*[18]

Discretionary CDDA decisions are not subject to external merits or (subject to the comments below) judicial review. However, they are subject to the principles of ethical and defensible decision making (such as procedural fairness and providing adequate reasons) and, since 1 May 2015, the Scheme and individual complaints are overseen by the Inspector-General of Taxation as 'Taxation Ombudsman'.

The Department of Finance's *Scheme for Compensation for Detriment Caused by Defective Administration, Resource Management Guide No 409 (November 2018)* makes the following comment about judicial review:

> *93. As CDDA Scheme decisions are not made under an enactment or law, decisions are not amenable to judicial review under the Administrative Decisions (Judicial Review) Act 1977. However, they may be subject to judicial review under section 75 of the Constitution or section 39B(1) of the Judiciary Act 1903.*

[16] (1977) 137 CLR 396 at 406 - 407,
[17] Background, paragraph 11
[18] Attachment A, paragraph 4

While a dissatisfied CDDA claimant could seek judicial review under the Constitution or the Judiciary Act, the Review is only aware of one such application[19] relating to the CDDA Scheme and that case has just commenced in March this year.

Any such action will involve significant legal costs and, if successful, limited outcomes:

> *In the ordinary course of a successful application, a court will not remake the decision for the Commonwealth agency, but most likely will quash (set aside) the decision and remit the decision [to the agency] to be made 'according to law', that is in accordance with the Court's judgment*.[20]

As a practical matter, very few small businesses would have the financial resources to pursue this form of review nor would the size of most CDDA claims for defective administration justify it.

In summary, as an executive scheme, CDDA permits discretionary redress based on the concepts of equity and moral obligation as a mechanism of last resort when no other remedy is available (other than act of grace) but some harm or loss has been suffered as a result of defective administration.

3.3 Authority

Portfolio Ministers have responsibility for decisions made under the CDDA Scheme. Resource Management Guide No 409 says:

> *7. Portfolio ministers decide applications made under the CDDA Scheme. A portfolio minister may authorise an official in a portfolio entity to consider and decide applications under the CDDA Scheme.*
>
> *8. The minister's authority is to be conferred expressly and must be given separately from the minister's general authorisation to incur expenditure. This requirement is in recognition of the special and potentially sensitive nature of decisions made under the CDDA Scheme for which the entity and its minister may be held accountable.*[21]

The Review understands that some Ministers have elected to make CDDA decisions personally while most of them authorise officials in their portfolio to investigate claims and make decisions on their behalf.

The Review also understands that management of the CDDA Scheme by Ministers and agencies across the Commonwealth varies considerably. Some Ministers require regular updates on, or information about, CDDA claims and may make some decisions themselves. Other Ministers have little direct involvement. It is a matter of personal preference.

The Inspector-General of Taxation (as 'Taxation Ombudsman') cannot investigate action taken by a Minister.

[19] The application has been brought under the Judiciary Act

[20] *Overview of Judicial Review mechanisms available in the Federal Court* delivered at a Commercial Bar Judicial Review Seminar by Emily Nance

[21] Resource Management Guide No 409, Part 1 – the CDDA Scheme

3.4 Agent of the Minister

The Resource Management Guide states:

> *9. Where a decision-maker is a person other than the portfolio minister, the decision-maker acts for and on behalf of the relevant minister, that is, the decision-maker is an agent of the minister and not a delegate. Only the portfolio minister or authorised official can decide claims under the CDDA Scheme.*[22]

The agency relationship between the Minister and the decision maker under the CDDA Scheme is quite different to the delegation of statutory decision making powers. In those cases, the Minister and the relevant department or agency will maintain protocols to ensure there can be no suggestion of ministerial interference in, or inappropriate influence on, a delegated decision.

However, as an agent of the Minister, it can be appropriate and in some cases recommended for an official to consult with the Minister on CDDA matters.

These considerations come into sharp focus where secrecy provisions are involved. The Tax Administration Act includes secrecy provisions to protect citizens' tax information which carry criminal penalties if contravened. Division 355-55 of the Act contains a specific exception to the secrecy provisions to facilitate disclosure of CDDA matters to the Minister. That provision allows for disclosure to the Minister if:

> … *the record or disclosure is for the purpose of informing decisions made under the Scheme known as the Compensation for Detriment Caused by Defective Administration Scheme*.

3.5 Summary

Given all of these factors, it is the Review's opinion that good practice in the management of CDDA claims in the ATO would involve briefing and conferring with each new portfolio Minister with CDDA Scheme responsibility in regard to:

- the Minister's primary role in relation to the Scheme and potential accountability for CDDA decisions
- fresh authorisations for specific ATO officers to investigate CDDA claims and make CDDA decisions as agents of the Minister within specified limits
- the Minister's instructions and guidance about the administration of the CDDA Scheme on the Minister's behalf, and
- how the ATO proposes to administer and report on the Scheme in accordance with the Minister's instructions and guidance (if any) and Finance's Resource Management Guide No 409.

[22] Ibid

Recommendation 1: That good practice in the management of CDDA claims in the ATO would involve briefing and conferring with each new portfolio Minister with CDDA Scheme responsibility in regard to:

1.1 the Minister's primary role in relation to the Scheme and potential accountability for CDDA decisions

1.2 fresh authorisations for specific ATO officers to investigate CDDA claims and make CDDA decisions as agents of the Minister within specified limits

1.3 the Minister's instructions and guidance about the administration of the CDDA Scheme on the Minister's behalf, and

1.4 how the ATO proposes to administer and report on the Scheme in accordance with the Minister's instructions and guidance (if any) and Finance's Resource Management Guide No 409.

SECTION 4: THE AUSTRALIAN TAXATION OFFICE AND SMALL BUSINESS

The Australian Taxation Office's purpose and strategic objectives are set out at the front of its 2017-18 Annual Report[23].

> *The ATO purpose is to contribute to the economic and social wellbeing of Australians by fostering willing participation in the tax and superannuation systems.*

Its first objective is:

> *The government and the public have trust and confidence in the integrity of the ATO.*

The Commissioner of Taxation regularly explains how taxpayer participation and cooperation are essential in a successful self-assessment tax system. In a speech to the Tax Institute's 30th National Convention, he said:

> *Levels of willing participation in Australia are high – with the vast majority of people willing to do the right thing. We know that people are more willing to comply if it is easy for them to do so, and if they have confidence that others are complying.*
>
> *Many things influence people's attitudes to paying tax: fairness, complexity, social norms, personal beliefs, economic conditions, advice and their relationship with their tax practitioner and the experience they have with the ATO.*[24]

Given the importance of small businesses in the Australian economy, their perceptions about fairness and their overall experience in dealings with the Tax Office are major factors in achieving the ATO's objective.

4.1 The definition of small business

There is no consistently used definition of small business across government. The ATO adopts this definition which fits squarely with the terms of reference for this Review:

> *An entity with an Income Tax or Activity Statement return in the last 3 years, with greater than zero and less than $10 million*[25] *business expenses or income but excluding:*
>
> - *Entities in Public Groups and Internationals population*
> - *Individuals without business income*

[23] Page 3

[24] *Reinventing the ATO,* 19 March 2016, pages 1-2

[25] This figure is, since 2016, the maximum turnover for businesses claiming small businesses tax concessions. It was previously $2 million

- *High Wealth Individuals and Wealthy Australians*

- *Superannuation Funds.*

The more commonly used Australian Bureau of Statistics definition has been neatly described in these terms:

> *The ABS defines small businesses as all entities that are independent and privately owned, are managed by an individual or a small number of persons, and have less than twenty employees. This choice reflects the greater availability of data that can be analysed using this definition.*[26]

Irrespective which definition is used, small business is important.

4.2 Small business – statistics and characteristics

The Tax Office publication *Small business by the numbers* contains a succinct but comprehensive summary of Australian small businesses which fall within the ATO's criteria. It discloses that, in 2016-17:

- small businesses contributed more than $380 billion to the Australian economy

- Australia has 3.8 million small businesses and their concentration correlates with the distribution of the general population

- those businesses comprise 44% (1.6 million) sole traders; 26% (980,000) companies; 21% (800,000) trusts; and 9% (330,000) partnerships

- 57% of small businesses are less than 10 years old

- small businesses employ around 5.2 million employees: 78% have no employees; 15% have 1-4 employees; 6% have 5-19 employees; and 1% have 20+ employees

- small businesses contribute 15% of total income tax (including fringe benefits tax) and 28% of total goods and services tax

- 69% of small businesses have a turnover less than $75,000; 14% between $75,001 and $200,000; 9% between $200,001 and $500,000; 4% between $500,001 and $1 million; 2% between $1 million and $2 million; and 2% between $2 million and $10 million

- the average annual turnover by entity type is: $341,856 company; $230,537 trust; $198,593 partnership; and $59,872 sole trader

- 71% of small business tax is paid on time: 16% is paid within 90 days; 3% is paid between 90 and 365 days; and 10% was not paid, and

[26] *The Economic Trends, Challenges and Behaviour of Small Businesses in Australia* by Sam Nicholls and David Orsmond, Reserve Bank of Australia Conference 2015, page 2, 2015

- small businesses owe 63% ($15.1 billion) of the ATO's collectable debt and 26% of that amount ($3.9 billion) is under a payment arrangement.

The ATO information sheet is attached at **Appendix 3**.

The most common small businesses:

> *… can be loosely grouped into three broad categories. One part of the sector provides a range of professional services to other businesses and households. This sector includes, among others, tradespeople (eg electricians and plumbers), skilled professionals (eg lawyers and accountants), doctors and health practitioners, real estate and insurance agents, and tourism-related businesses. Another segment includes various types of retail outlets (eg grocers, hairdressers, bars and restaurants). Finally, there are a number of firms that produce a range of niche and other goods in the manufacturing, construction and agricultural industries.*[27]

Since it was launched on 11 March 2016, the Australian Small Business and Family Enterprise Ombudsman's statutory functions have included advocating for and assisting small businesses and family enterprises.[28] In its first year of operation, the ASBFEO published an assessment of the economic importance of small business which made the following points[29]:

- *the size of a business is an important determinant of business longevity. The small business sector is very volatile, with non-employing small businesses having the lowest survival rate of all businesses in Australia*

- *small business is the least assisted sector of the economy. Only 15 percent of small businesses report receiving any form of government assistance, compared to 30 percent of medium businesses and 57 percent of large businesses,* and

- *a healthy small business sector is a prerequisite for a growing economy with high employment opportunities.*

In relation to the first of those three points, Tax Office data shows that:

- *almost half of small businesses are under financial pressure within the first year of starting business and this pressure increases in years one to three*

- *more than 60% of small businesses cease operating within three years of starting, and*

- *90% of small business failures are due to poor cash flow*.[30]

[27] Ibid
[28] Australian Small Business and Family Enterprise Ombudsman Act 2015, section 13
[29] *Small Business Counts – Small Business in the Australian Economy*, Overview
[30] *Tax in a changing world – change is the new black*, paper delivered by Second Commissioner Andrew Mills at the Australasian Tax Teachers' Association 31st Annual Conference, 17 January 2019

ATO data also shows that:

> *Small businesses who interact with the ATO generally do so via an intermediary, with 88% of tax returns, and 45% of Activity Statements, lodged by a tax agent*.

Those facts and statistics taken together suggest the following general propositions:

- small business proprietors may lack training and experience in business administration including cash flow management and taxation compliance (particularly in complex areas of tax law such as research and development grants, superannuation, goods and services tax and personal services income)

- small businesses are likely to be undercapitalised

- personal assets (such as the family home) are likely to have been put at risk as the only available source of funding for a small business

- small business proprietors are likely to be time poor and have limited time available to deal with detailed compliance obligations away from the day-to-day demands of their business, and

- for small business people, dealing with, for example, a Tax Office audit can be a very confronting experience given what the ASBFEO has called the ATO's *unparalleled authority in terms of its resources, administrative powers and legal expertise.*[31]

The Commissioner of Taxation acknowledged some of the pressures on small business taxpayers in his evidence to the Senate Economics Legislation Committee on 30 May 2018 when he said:

> *This dispute assist service recognises that some taxpayers whose business may not be going well are also sometimes going through other stressful issues in their lives, such as family break-up, or physical and mental health issues*.[32]

The Review is aware that, over the past five or so years, the Government and the Tax Office have introduced a considerable number of measures to assist small businesses in their dealings with the ATO taking into account the propositions set out above. Some of those measures are noted in Section 9.

4.3 Perceptions of the CDDA Scheme

The terms of reference require the Review to address perceptions that the CDDA Scheme does not adequately compensate small business taxpayers for the effect of defective administration and the Review has sought a range of opinions on that issue. The Review has also considered the perceptions identified in earlier reviews of, or investigations into, the CDDA Scheme or which touched on it.

[31] ASBFEO's submission to The Treasury's *Small Business Dealings with the Australian Taxation Office* inquiry, May 2018, Executive Summary, point 1

[32] Hansard, Senate Economics Legislation Committee, page 11

The list below sets out regularly mentioned perceptions of the Scheme that came to the Review's attention:

- the Scheme lacks transparency
- the definition of defective administration as applied by the ATO is too narrow and too legalistic
- the decision maker within the ATO is not seen to be sufficiently independent[33]
- there is very limited opportunity for internal review of a CDDA decision and, again, the process is not seen to be sufficiently independent[34]
- there is no avenue for binding external review as the Ombudsman (historically) and the Inspector-General of Taxation (now) can only make non-binding recommendations to the ATO
- the Scheme is not widely known (which may account for the small number of claims)[35] and the ATO is not doing enough to ensure taxpayers and their advisers are aware of the Scheme
- the amounts of compensation are small and calculated in a legalistic way rather than in the intended spirit of moral obligation or fairness
- in many cases, the expectation of low amounts of compensation (if any) can lead taxpayers or their advisers to decide it is not worth the time, effort and possibly professional costs[36] to make a CDDA claim
- successful claimants are often required to enter into a confidentiality agreement which limits public discussion about the types of claims which are accepted as defective administration, and
- the Scheme is flawed because it does not cover defective administration by Commonwealth contractors.[37]

These perceptions are said to discourage CDDA claims on the ATO. If that is so, it follows that the Tax Office's claims statistics are not a reliable guide to the potential need for, and use of, the Scheme if the identified shortcomings were, where justified, addressed.

There has been a considerable consistency in many of the perceived shortcomings in the Scheme over a long period of time as a cursory inspection of the documents listed in Appendix 2 will show. Some of the

[33] In some instances, the ATO has been described as *judge, jury and executioner*

[34] ASBFEO has postulated that ATO review officers adopt same interpretative statements and cultural norms underlying the original decision and are therefore unlikely to produce a different result: Submission to the Treasury Review May 2018, Executive Summary, paragraph 6

[35] This issue (which includes difficulty accessing information about the Scheme electronically) was noted by the Australian Chamber of Commerce and Industry and mentioned by many others

[36] Resource Management Guide No 409, paragraph 71 generally excludes payment of professional costs in making a CDDA claim

[37] Resource Management Guide No 409, paragraph 16

perceived shortcomings are more contemporary, such as concerns that the CDDA does not explicitly cover compensation for ATO technology failure and IT outages.[38]

For example, in the 1999 report of an own motion investigation, *To Compensate or Not to Compensate,* the Ombudsman commented:

> *6. There is no common understanding or acceptance of what constitutes standards of service and administration acceptable to the government and the community. Consequently, there are no generally accepted standards for measuring whether a compensation payment would be 'publicly defensible', a requirement for compensation for defective administration,* and
>
> *8. Our impression is that agencies believe that we recommend compensation too readily, without understanding the constraints under which they operate. By contrast, we believe agencies could provide compensation more often than they do, by adopting a more flexible, customer focused approach based on a broad interpretation of the powers available to them and by reference to standards they set themselves, for example, in their service charters.*[39]

The Department of Finance conducted a *Review of the Compensation for Detriment Caused by Defective Administration Scheme* in 2004-05. In a submission to that review, the Ombudsman noted that:

> *… most issues arise from the administration of Finance's CDDA guidelines by agencies, rather than the content of the guidelines themselves.*

The Ombudsman also identified several areas of complaint including alleged:

- *rejection of claims at an inappropriate level in agencies*
- *a tendency (without proper investigation) to prefer an agency's version of events to a claimant's,* and
- *inadequate reasons explaining why a claim had been rejected*.[40]

In 2009, the Ombudsman said in a general review of the Scheme:

> *Agencies need to provide staff with clearer guidance, with a less legalistic approach, and to emphasise more strongly the administrative and discretionary nature of the CDDA Scheme and the moral obligation that underpins it*.[41]

The Senate Legal and Constitutional Affairs Committee considered the CDDA Scheme (among others) in its *Review of Government Compensation Payments* in 2010. The Committee noted concerns raised in submissions including *that 'detriment' is defined too narrowly under the [CDDA] scheme and that the threshold for demonstrating economic loss is too high*.[42]

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[38] Technology and IT concerns were raised by CPA Australia Ltd, Chartered Accountants Australia and New Zealand and the Institute of Public Accountants

[39] Executive Summary, paragraphs 6 and 8

[40] Report, Part 4

[41] *Putting things right: compensating for defective administration*, August 2009, paragraph 3.6

[42] Paragraph 3.46(a)

In its 2016 *Review into the Taxpayers' Charter and Taxpayer Protections,* the Inspector-General of Taxation commented:

- *In cases where taxpayers have succeeded in meeting the threshold criteria, submissions made to the IGT have observed that the CDDA Scheme does not adequately address productivity loss, opportunity costs (particularly for tax practitioners) or psychological injury (for example, stress and depression)*[43]

- *The manner in which the CDDA Scheme is administered has given rise to perceptions of bias and lack of independence. This perception stems from having the ATO form its own opinion as to whether its actions amount to defective administration and deciding the appropriate quantum of compensation for taxpayers. There is a strong view that having the ATO review and decide on the outcomes of matters that it has purportedly mismanaged is lacking in basic procedural fairness*[44], and

- *Some stakeholders have viewed the limited number of CDDA claims approved and low quantum of CDDA Scheme payments as an indication that it is 'just a token scheme' and in place 'for the sake of having a compensation scheme'.*[45]

More recently, the House of Representatives Standing Committee on Tax and Revenue published its review of the ATO's 2016-17 Annual Report in February 2019. The review of the Annual Report was extended to become a *Fairness, functions and frameworks – performance review*.

The Committee noted:

> *The IGT has recognised compensation as a 'difficult issue for the ATO', with the ATO's admission of fault and the level of compensation awarded a 'sticking point' for resolution of these claims*.[46]

The Committee made this recommendation:

> *The Committee recommends the Government should review and publicly consult on proposals to establish a new and dedicated scheme for consideration of compensation claims against defective tax administration to reduce perceptions of conflicts of interest and improve taxpayer confidence in the fairness and probity of decisions made*.[47]

As a result of its investigations, the Review acknowledges that the perceptions identified in this Section indicate continuing concerns with the structure of the CDDA Scheme and its administration by the ATO which require careful consideration.

In doing so, the Review is aware that some of these perceptions have been, or are being, addressed through initiatives introduced by the Commissioner over the last few years.

[43] Paragraph 4.31
[44] Paragraph 4.54
[45] Paragraph 4.58
[46] Report, paragraph 4.61
[47] Report, Recommendation 14, paragraph 4.67

While not directly related to the CDDA Scheme, it is worth noting that the ATO commenced measuring perceptions of fairness in response to the House of Representatives Tax and Revenue Committee's inquiry into tax disputes. Taxpayers' perceptions of fairness in tax disputes have increased from 49% in 2014 to 65% in 2017-18 and that research has helped shape the ATO's approach to dispute resolution.

Recent reforms and further possible solutions are considered in later Sections of this Report.

SECTION 5: ANALYSIS OF THE ATO'S CDDA CLAIMS

When the CDDA Scheme was established in 1995 it was envisaged that:

> *The number of cases warranting approval of compensation for detriment because of agency maladministration is fairly small. Indeed, most agencies would rarely encounter the issue.*[48]

This statement was mainly based on the expectation that most CDDA claims would be made against a handful of Commonwealth agencies dealing directly with the public and this has proved to be the case. The agencies which receive the large bulk of CDDA claims are the ATO, the Department of Human Services (through its Centrelink, Medicare and Child Support programs) and the Department of Home Affairs.

The following table sets out a comparative summary of those agencies' CDDA statistics for the last financial year.

Table 2: Three agency comparison of CDDA statistics 2017-18

	ATO	DHS	Home Affairs
Number of claims lodged	171	1,616 (inc. legal liability)	161
Number of approved/paid claims	76	724	90
Total amount paid for CDDA claims	$409,035	$2.737 million	$372,918
Completion service targets	56 days	90 days	Not recorded

Source: This table comprises a compilation of information from each agency

The table below provides a snapshot of the ATO's total CDDA statistics for the last five years comprising all claims for detriment caused by defective administration, not just claims from small business.

[48] Cabinet submission 2207, paragraph 15

Table 3: Five year snapshot of ATO total CDDA statistics

	2013-14	2014-15	2015-16	2016-17	2017-18	Totals
Number of claims received	216	192	160	190	171	929
Number of claims finalised	219	201	160	192	166	938
Number of approved claims	79	77	59	79 +17*	76	387
Total amount paid	$841,754	$738,402	$317,502	$801,305	$409,035	$3.1m
Average payment	$10,655	$9,590	$3,414	$8,435	$7,575	
Median payment	$300	$484	$424	$500	$495	

Source: Australian Taxation Office Annual Reports. *The 17 additional payments were made as a result of a streamlined claim process

However, this Review is limited to a consideration of CDDA claims by small business (that is, entities with an annual turnover of less than $10 million).

General Counsel lawyers manage all CDDA claims and assist with Act of Grace matters. They do not record claimants' annual turnover as there has been no need to do so.[49] In these circumstances, they provided the Review with small business claims information to the best of their ability.

General Counsel lawyers examined the last five years' CDDA claims and identified 289 cases which they judged fell within the terms of reference.

Table 4: Total number of ATO small business CDDA claims completed from 1 January 2014 to 31 December 2018

Year	Number of claims	Total approvals (in full, in part, and offered but not accepted)	Total refused	Withdrawn or application not complete
2014	49	15	32	2
2015	48	15	32	1
2016	67	20	39	8
2017	81	30	49	2
2018	44	19	22	3
Totals	**289**	**99**	**174**	**16**

Source: Australian Taxation Office

[49] In any event, such data would have been of limited assistance as the annual turnover limit for small business concessions was $2 million until it was increased to $10 million in 2016

The ATO used to list the categories of defective administration specified in CDDA claims on hand in the last month of the financial year but it has not done so since 2014-15. The following details were published before that change took place[50]:

- in 2013-14 the most common categories were: unspecified; dispute over audit action; ATO officer error/delay; and incorrect advice, and

- in 2014-15: ATO officer error/delay; dispute over audit action; systems error/delay; incorrect advice; and unspecified.

General Counsel provided data about the most common types of claims for compensation in the following three years to 2017-18. They were ATO officer error or delay; system error or delay; dispute over audit action; and incorrect advice.

As noted earlier, General Counsel gave the Review a spreadsheet setting out the basic details of 50 approved small business claims and a second spreadsheet comprising 50 refused claims processed over the last five years.

The main categories of defective administration identified in the approved claims were recorded as:

- delay

- failure to follow proper procedures

- IT systems issue or computer processing error, and

- incorrect information or advice.

The compensation payments made in the approved cases were calculated principally with reference to:

- professional fees incurred by the claimant in dealing with the defective administration (but not in preparing the CDDA claim)

- additional costs incurred as a result of the defective administration (lost interest, bank fees and other costs being a direct result of the defective administration), and

- claims by third party tax agents or other professional advisers for costs incurred by them as a result of the defective administration.

There are four points to note about those compensation payments:

- the direct detriment caused by the defective administration was easily identified and then quantified (from invoices, bills, receipts and so on)

[50] See the Compensation Statistics Appendix in the relevant Annual Report

- the largest compensation payment for professional fees was $68,312 (against a claim for $102, 972) and the smallest payment was $7.50 (being the amount claimed)

- none of them include any payment for the more complex financial detriment some applicants claimed to have suffered in a lengthy dispute with the ATO, and

- none of the 50 payments included compensation for non-economic loss.

While the payment of $7.50 may come as a surprise, small claims and payments are common. In 2011, the Department of Finance conducted a survey of the operation of the CDDA Scheme in government agencies. The ATO's completed response to the questionnaire was forwarded to Finance under cover of a letter dated 10 May 2011. It included a 16 page spreadsheet of compensation payments made in 2008, 2009 and 2010. Nearly four pages of the spreadsheet were taken up with payments less than $100, starting at $6.

The defective administration alleged in the 50 refused claims was more diverse. By way of example, there were:

- claims which clearly fell outside the scope of the CDDA Scheme (such as claims for compensation for the personal time involved in dealing with the ATO)

- claims in which defective administration was established but no detriment was sustained

- some claims for professional fees

- claims arising from audits where ATO officers were assessed to have acted appropriately and in accordance with proper procedure, and

- claims that are difficult to categorise due to their diverse circumstances and multiple allegations of defective administration which often compounded over time.

If a claimant is dissatisfied with the outcome of a CDDA claim, there is the possibility of an internal review or a reconsideration. Resource Management Guide No 409 states:

> *88. It is open to entities to determine whether to implement formal internal review mechanisms for decisions made under the CDDA Scheme.*
>
> *89. Entities may also choose to determine whether reconsideration is warranted on a case-by-case basis.*
>
> *90. If a claimant provides pertinent new evidence, facts or argument to support their application, reconsideration may be appropriate.*

General Counsel provided the following details about internal reviews.

Table 5: Internal reviews of CDDA decisions 2014 - 2018

Year	Number of Reviews	Upheld	Varied
2014	1	1	
2015	2	2	
2016	2	1	1
2017	3	1	2
2018	6	5	1
Total	**14**	**10**	**4**

Source: Australian Taxation Office

A disgruntled claimant can seek assistance from the Ombudsman.

The Commonwealth Ombudsman dealt with CDDA complaints from 1995 to 2015 and commented extensively on the CDDA Scheme and its administration in two major own motion investigations in 1999 and 2009.[51]

Since 1 May 2015, dissatisfied claimants may lodge a complaint with the Inspector-General of Taxation (in its extended role as 'Taxation Ombudsman') regarding CDDA decisions made by the ATO. General Counsel supplied the following details about complaints lodged with the IGT.

Table 6: Complaints about CDDA claims referred to the IGT (as 'Taxation Ombudsman')

Year complaint received	Number of referrals	Affirmed	Recommendations	Recommendations made
2015	4	2	1	CDDA decision to offer compensation, client declined offer. IGT recommended offer is re-made to applicant with an 'overarching letter of apology'.
2016	8	5	1	IGT requested the ATO write to the claimant to confirm that an issue uncovered as part of the IGT investigation that was not considered in the original decision did not amount to defective administration.

[51] See Appendix 2

2017	9	6	1	IGT recommended the ATO reconsider whether compensation was payable in relation to four discrete issues identified after the internal review.
2018	2		1	IGT recommended ATO make further efforts to engage with complainant about offer of settlement.
Total	23	13	4	

General Counsel advised that the complaints listed above concern the process of claiming compensation or the decision made on a CDDA claim. They do not include complaints where compensation may only have been mentioned by the complainant or the IGT as a possible remedy.

The ATO is not always aware that a complaint has been made to the IGT or given detailed information about the complaint or its outcome.

While General Counsel officers are all lawyers, the Office of General Counsel does engage external legal assistance from time to time to manage a fluctuating workload or to deal with a complex matter. General Counsel provided the following information about external legal expenditure on small business CDDA matters.

Table 7: The ATO's external legal expenditure on small business CDDA matters

Year	2014-15	2015-16	2016-17	2017-18	2018-19 (31 December)	Total
Number of matters	3	3*	1	1*	0	8
Total costs**	$88,696.35	$80,467.14	$9,468.93	$87,991.49	$99,879.00	$366,502.91

*Includes separate phases of the same matter with new phases briefed as new matters in separate years. **These figures include the total amounts paid in the financial year noting that some matters have carried across multiple years

The statistics from General Counsel provide a useful picture of the nature, composition and volume of ATO's CDDA claims and workload over the last five years. The following analysis of the General Counsel data[52] gives some indication of the likely use of the CDDA Scheme by small business and its outcomes over that period:

- a total of 387 out of 929 claims (41.65%) were accepted and received compensation payments totalling $3,107,913

[52] Table 3 and the list of 50 approved applications

- a total of 542 claims (58.35%) were not approved because they did not come within the Scheme, there was no defective administration or no detriment

- General Counsel has estimated that 289 of the total 929 claims (31.10%) were made by small business

- applying the same percentage of approved claims (41.65%), 120 of the 387 approved claims (31%) were made by small business claimants

- 31% of the total compensation payments over five years comes to $963,453 (less than an average of $200,000 a year) but the compensation paid to small business was probably less than that figure due to the large number of small payments, and

- 27 of the 50 successful small business claims on the list provided by General Counsel received compensation payments less than $1,000 including five cases of compensation less than $100.

The limited use of the CDDA Scheme by small business and the low compensation payments are less than one would expect given the volume of business conducted by the ATO. On 30 May 2018, the Commissioner told the Senate Economics Legislation Committee:

> *We are a large organisation. We run complex tax and superannuation systems. We have around 17 million tax returns lodged each year, and when you add in the BAS and activity statements, the number of lodgements is over 35 million. In such a large system human error will inevitably result in mistakes being made …* [53]

[53] Hansard, Senate Economics Legislation Committee, page 11

SECTION 6: THE ATO'S CDDA PROCEDURES

All compensation claims for detriment caused by defective administration are investigated and, with very few exceptions, decided in the Office of General Counsel. CDDA claims are processed in accordance with the ATO's CDDA General Counsel Manual and Finance's Resource Management Guide No 409. There are informal processes of consultation about CDDA claims between General Counsel and other ATO areas or business lines which support the documented procedure.

There are four steps involved in determining a CDDA claim: determine if the Scheme applies; ascertain if there has been defective administration; identify if the claimant has suffered detriment directly resulting from the defective administration; and quantify the financial loss (including opportunity costs) taking the claimant's own actions into account.[54]

The Review has carefully considered the General Counsel Manual (which has electronic links to other relevant ATO information) and:

- decision templates
- a sample of decision letters sent to claimants
- a random selection of case files
- the statistics and other details set out in Section 5, and
- information about specific cases drawn from various sources.

In addition, the Review has consulted with lawyers from the Employment Law and Customer Compensation Branch of the Legal Services Division in the Department of Human Services and compared their Customer Compensation Manual.

The Review also spoke to the Discretionary Compensation Team in the Civil Commercial and Employment Law Branch in the Department of Home Affairs.

The Review's overall assessment is that current ATO procedure appears to work well in relation to claims where there is clear evidence of the defective administration and resulting detriment. This view is evidenced by the following statistics:

- in 2017-18, 92% of 87 completed claims were finalised within the 56 days performance standard and 90% of another 64 completed claims with a negotiated time frame were finalised within the agreed period[55], and

[54] See Resource Management Guide, paragraphs 75 and 76
[55] ATO Annual Report 2017-18, Appendix 5

- 50% of the cases on the spreadsheet of approved claims provided by General Counsel[56] were paid at the (often small) amount claimed.

However, the Review recommends the ATO's procedure be further developed and documented in a more comprehensive CDDA Manual. The Review considers that more thoroughly defined procedures would form the basis for managing and assessing General Counsel's handling of CDDA claims and assist new starters in undertaking CDDA work.

The proposed enhancements could also address some aspects of the adverse perceptions set out in Section 4.

6.1 Categorisation of claims for compensation

The current procedure does not differentiate between straight forward claims and more complicated claims with detailed factual circumstances and possibly multiple allegations of defective administration over a sometimes lengthy period.

An analysis of General Counsel's list of 50 approved small business claims shows that:

- in 23 cases, the ATO paid out the exact amount of compensation requested by the claimant

- in 16 of those 23 cases, the compensation paid was less than $1,000 and in 12 of those 16 cases the compensation was less than $500 (the lowest payments being $36, $27.50, $24 and $7.50), and

- the majority of the 23 cases involved a straight forward claim for professional fees incurred as a direct result of the defective administration and the remainder were mainly for bank fees and out-of-pocket expenses.

As pointed out earlier in this Report, small payments of compensation have been a striking feature of the CDDA Scheme across the Commonwealth for a long time and the Review assumes they will continue.

In these circumstances, the Review considers there would be advantage in allocating incoming claims on receipt by General Counsel into three categories along the lines set out below. The proposed categorisation of a particular matter is not intended to be rigid and could be changed, if appropriate.

In regard to classification, the amount claimed in compensation is an indicator to be taken into account but it is not a determining factor by itself. Many claims do not specify an amount. In other cases, a large amount is claimed but all or significant elements of the alleged defective administration or detriment clearly do not come within the ambit of the CDDA Scheme.

The categories are:

- category 1: straight forward claims where the defective administration and the detriment (if any) are readily identified and quantified (such as professional fees incurred in responding to

[56] See Section 5

the defective administration or lost interest on a delayed payment) and it is likely that the ATO will pay out the amount of compensation requested by or promptly agreed with the claimant

- category 2: standard claims which require more thorough investigation to determine defective administration or the amount of compensation to be paid (if any), and

- category 3: the very small number of complex, significant or sensitive claims requiring intensive effort and high level involvement.

The ATO procedure could then be adjusted to match the circumstances of the particular matter:

- category 1 claims would be assessed and decided quickly by General Counsel junior officers through an expedited process using telephone, emails and succinct correspondence

- category 2 claims would largely follow the current procedure subject to the other proposals set out below, and

- category 3 claims would be allocated to a senior General Counsel officer and receive close monitoring and the decision brief would be referred to a highly placed decision maker within the ATO consistent with the complexity, significance or sensitivity of the matter.

This approach is consistent with paragraph 73 of the Resource Management Guide:

> *In considering the type and amount of evidence required to substantiate the application, entities can take account of the nature and size of the compensation requested.*

6.2 Separate the investigation and decision making functions

At present, General Counsel officers investigate and make decisions in all but a few CDDA claims.

It is common practice in administrative review for the investigator to complete their task and then present a brief to an uninvolved more senior officer for decision. The Review considers there would be three advantages in adopting that procedure in category 2 and most category 3 claims:

- it accords with better administrative practice

- the separation of functions can make the investigator's dealings with the claimant easier if they are one step removed from the decision maker, and

- the impartial decision maker decides the case on its merits as presented in the decision brief without any preconceptions formed during the investigation.

6.3 Preliminary view and procedural fairness

In category 2 and 3 cases, the Review suggests that, when the investigator has reached a preliminary or tentative view on a claim, they should provide details of that view to the complainant for comment before the decision brief is finalised.

This suggestion meets the disclosure requirement set out in paragraph 51 of the Resource Management Guide:

> *… Procedural fairness requires that the substance of documents (relevant to the claim) held by the entity but not known to the claimant is shared with the claimant.*

It is also in line with the Ombudsman's 2009 report which recommended that agencies:

> *… ensure claimants have a full opportunity to comment on the agency's assessment of a claim prior to a decision being made.*[57]

The Review understands that this process occurs in some but not all category 2 and 3 cases. The more common process appears to be that the General Counsel investigator/decision maker sends the finalised decision and, if required, a deed of release. If the claimant rejects the decision or the compensation offered is not acceptable, General Counsel can, on occasions, reconsider the claim and make a second offer.

This common ATO process does not consistently meet the requirements set out in paragraph 40 of the Resource Management Guide:

> *Prior to a decision being made on an application, the entity must ensure that the claimant is afforded procedural fairness. This includes, but is not limited to:*
>
> - *providing an opportunity for the claimant to present their claims or allegations in writing*
> - *providing an opportunity for the claimant to view and comment on adverse material that will be considered by the decision maker, and*
> - *making a decision that is free from bias.*

6.4 Internal review

The Resource Management Guide contemplates both reconsideration of a decision and internal review.

Reconsideration involves a decision being reconsidered by the original decision maker. The ATO may determine whether a reconsideration is warranted on a case by case basis if the applicant provides pertinent new evidence, facts or argument to support their application.[58]

Internal review is a different, more formal process. An internal reviewer considers the decision made by the original decision maker and the information and evidence on which that decision was based. No new material is taken into consideration.

The Resource Management Guide provides in paragraph 88 that:

> *It is open to entities to determine whether to implement formal internal review mechanisms for decisions made under the CDDA Scheme.*

[57] *Putting things right: compensating for defective administration,* recommendation 1(i). page 34
[58] Paragraphs 89 and 90

There were only 14 internal reviews of CDDA claims in the five years to 30 June 2018.[59] The Review suggests the ATO should take a more liberal approach to offering, and accepting requests for, internal review of decisions on claims in categories 2 and 3.

The Review considers that the more ready availability of internal review of CDDA decisions would accord with good administrative practice. It would also go some way to redressing the perception that decision making within General Counsel is a closed shop that needs to be more open and transparent.

In most cases, the Review expects a more senior, duly authorised officer from another ATO business line or area (that is, not within the Office of General Counsel) would be an appropriate internal reviewer. In those cases, the internal reviewer would make the final decision.

In a very small number of category 3 cases, it may be appropriate for the internal reviewer to be an independent person brought in from outside the ATO to conduct a particular review. At various times, there have been suggestions that the Ombudsman or the Inspector-General of Taxation could perform this task. Both of them have rejected that proposal as incompatible with their long-established complaint handling and recommendatory functions.

The selection and authorisation of an independent reviewer could be done on a case-by-case basis (possibly from an approved panel) or an independent reviewer could by appointed for a set period and be available to undertake reviews when required.

Two examples of independent review arrangements are:

- the Pharmaceutical Benefits Independent Review Scheme: under that scheme, the independent reviewer's findings and recommendations are reported to the Pharmaceutical Benefits Advisory Committee and, after reconsideration, by the Minister for Health as part of a complex scheme for listing drugs on the Pharmaceutical Benefits Scheme, and

- the Independent Review of Adverse Security Assessments[60]: the independent reviewer reviews adverse security assessments issued by the Australian Security Intelligence Organisation to persons who remain in immigration detention and have been found to be owed protection obligations under international law. The reviewer works on a part-time basis when required and reports findings and recommendations to the Director-General of Security. The Director-General makes the final decision whether to maintain or vary the adverse security assessment. The independent reviewer reports annually to the Parliament in an appendix to the ASIO annual report.

If an internal review is conducted by an independent reviewer, the reviewer's findings and recommendations should be submitted to the Commissioner for determination. A compensation claim could involve millions of dollars and, in the Review's opinion, the Commissioner should make the final decision because:

- the payment has to be publicly defensible and the Commissioner is in the best position to make that assessment, and

[59] See Section 5

[60] Robert Cornall AO is the Independent Reviewer of Adverse Security Assessments

- the Commissioner is ultimately responsible for the proper expenditure of the ATO's budget appropriation.

However, to ensure the process is transparent, the independent reviewer should make an annual report to Parliament[61] on any reviews conducted during the year and the Commissioner should report on their final outcomes.

6.5 Too legalistic approach

A regular criticism of the ATO is that it takes a too legalistic approach in its handling of CDDA claims. In 2009, the Ombudsman found (and confirmed findings identified in earlier reports) that there is a need for:

> … *less defensive and legalistic approaches to CDDA decision making by agencies.*[62]

Some of the files and letter templates looked at by the Review contain detailed consideration of the legal basis of the CDDA Scheme and its application to the claim under consideration. In some instances, judicial decisions were cited and relevant case extracts quoted. While this analysis underpins the ATO decision, it is more information than most claimants need.

The language used in General Counsel's documentation and decision letters is likely to be a major contributor to the perception that the ATO takes too legalistic approach to its investigation and determination of claims for discretionary compensation.

That perception could be addressed, at least in part, by redrafting General Counsel's documentation and correspondence with claimants and their professional advisers in more succinct, everyday language.

6.6 Regular CDDA reporting to the Commissioner

The ATO is a huge organisation and the Commissioner has very demanding responsibilities. Information is brought to the Commissioner's attention in the usual way by the ATO's business lines on a need to know basis.

However, the Review suggests the Commissioner should receive at a regular report on CDDA matters. The report would include statistical data on all categories of claims for compensation, trends and status reports on complex, significant or sensitive category 3 CDDA cases and possibly some category 2 cases.

The reasons for this recommendation are:

- the ATO's administration of the CDDA Scheme is the subject of constant attention as appears from Appendix 2, and

- the Review considers the Commissioner has a key role to play in addressing the adverse perceptions set out in Section 4.

[61] The independent reviewer's report could be an appendix to the ATO's Annual Report
[62] *Putting things right: compensating for defective administration*, Executive Summary

Recommendation 2: That the ATO further develop its procedures for handling claims for compensation in a more comprehensive CDDA Manual which includes:

2.1 categorising claims into three categories (straight forward; standard; and complex, significant or sensitive) with varying procedural requirements depending on the nature and circumstances of the claim.

2.2 separating the investigation and decision making functions for claims in categories 2 and 3.

2.3 providing the claimant with the opportunity to consider and comment on the investigator's preliminary view of claims in categories 2 and 3 before a decision is made.

2.4 taking a more liberal approach to offering, and accepting requests for, internal review of decisions in categories 2 and 3 if there appears to be a reasonable basis for it.

2.5 redrafting CDDA documentation and decision letters in more succinct, everyday language.

2.6 providing a regular report on CDDA matters direct to the Commissioner.

SECTION 7: CDDA SCHEME IMPLEMENTATION

Many of the criticisms of the CDDA Scheme (such as it is a *token* scheme) are about its interpretation and implementation rather than its structure.

In 1999, the Ombudsman conducted an own motion investigation of financial redress for maladministration. Although that investigation took place a long time ago, its findings are still significant. The Ombudsman's inquiry took place just four years after the CDDA Scheme commenced and provided a contemporaneous opportunity to assess if the Scheme was being implemented as intended.

The Ombudsman noted that:

> *… compensation mechanisms … can be interpreted broadly enough to enable agencies to pay compensation in all cases where they believe it is warranted, or narrowly enough to exclude any request, depending on the agency's approach to compensation generally or in individual cases*.[63]

The Ombudsman found that most difficulties were caused by:

> *… the approaches agencies use when applying the compensation mechanisms, rather than the mechanisms themselves.*[64]

This Section analyses several aspects of the Tax Office's interpretation and implementation of the CDDA Scheme which came to attention during the course of the Review.

7.1 The definition of defective administration

The first step in considering a CDDA claim is to determine whether there has been defective administration. Approaching the claim in two stages avoids the ATO and the claimant spending time (at least in factually complex claims) looking for and collating evidence of detriment if there was no defective administration.

The definition of defective administration has not changed since 1995. Defective administration is defined in both Attachment G to the 1995 Cabinet submission 2207 and the current Resource Management Guide[65] in these terms:

- *a specific and unreasonable lapse in complying with existing administrative procedures that would normally have applied to the claimant's circumstances*

[63] *To compensate or not to compensate*, paragraph 10
[64] Ibid, paragraph 16
[65] Paragraph 17

- *an unreasonable failure to institute appropriate administrative procedures to cover a claimant's circumstances; or*

- *giving advice to (or for) a claimant that was, in all the circumstances, incorrect or ambiguous; or*

- *an unreasonable failure to give to (or for) a claimant, the proper advice that was within the official's power and knowledge to give (or was reasonably capable of being obtained by the official to give).*

The issue is whether that long-standing definition adequately encompasses what can be fairly regarded as defective administration in the ATO's dealings with small business in 2019. The Commissioner set this goal for the CDDA Scheme in the ATO's Estimates hearing on 30 May 2018:

> *…we could probably be better at acknowledging our real mistakes, apologising, compensating for any actual financial loss and moving on*.[66]

In other words, do the Commissioner's 'real mistakes' come within the definition of defective administration as currently applied by General Counsel? If not, can that interpretation be broadened to encompass those mistakes or is a public service wide CDDA Scheme no longer fit for the ATO's purpose?

The Resource Management Guide provides some useful further explanation about unreasonable lapse or failure:

> *46. An unreasonable lapse or failure is one where the actions of the official(s) involved are considered to be contrary to the standards of diligence that the entity expects to be applied by reasonable officers acting in the same circumstances with the same powers and access to resources.*
>
> *47. Cases may arise where individual instances of administrative omissions or errors may not be regarded as unreasonable when considered in isolation from each other, but may constitute defective administration when considered in totality and in the context of the combined impact of the omissions or errors on the claimant.*

The Review is of the opinion that a number of problematic situations could be brought within the CDDA Scheme, if the Minister or the Commissioner chose to do so, using a combination of current or new ATO service, conduct or performance standards and paragraphs 46 and 47 of the Resource Management Guide.

Put simply, the Review is of the opinion the Commissioner can define 'defective administration' so it covers the ATO's 'real mistakes'.[67]

[66] Hansard, Senate Economics Legislation Committee, page 11
[67] See Section 9

7.2 The definition and quantification of detriment

Once defective administration has been established, the next step is to determine the detriment it caused as compensation is only available if the claimant has suffered detriment as a direct result of the defective administration.[68]

The definition of 'detriment' is:

> *Detriment is considered as the amount of quantifiable financial loss, including opportunity costs, that a claimant can demonstrate was suffered despite having taken reasonable steps to minimise or contain the loss. If, for some reason, it is impractical for a claimant to demonstrate all or part of the quantifiable loss, the decision maker may make whatever assumptions as to amount, including with respect to the claimant's actions to minimise or contain the loss, that are necessary and reasonable in the circumstances*.[69]

'Pure economic loss' means financial detriment unrelated to any damage or physical injury to the claimant or their property.[70] 'Non-economic loss' claims may relate to personal injury (including psychiatric injury), emotional distress or damage to reputation[71] but not solely for grief or anxiety, hurt, humiliation, embarrassment, disappointment, stress or frustration unless it is related to a compensable personal injury.[72] Compensation for personal injury loss is to be determined in accordance with legal principle and practice.[73]

Each claim is determined on its merits and, as these are discretionary payments, they do not set precedents for later applications for CDDA compensation.

The overarching principle in quantifying detriment is to restore the claimant to the position they would have been in had the defective administration not occurred.[74] There is no financial limit on the amount of compensation payable under the Scheme[75] but the payment must be publicly defensible.[76] Compensation is paid from the ATO's budget appropriation – there is no program funding for the CDDA Scheme.

As with defective administration, these provisions call for important judgments by the decision maker which can significantly affect the amount of compensation payable. For example:

- *assessing what detriment is the direct result of the defective administration*: assume payment of a large rebate to a small business is unjustifiably delayed for say six months despite several requests for payment and the delay has a severe impact on the small business' cash flow. Current practice would assess interest on that amount for that period and possibly refinancing costs to cover the unexpected shortfall in revenue. But what if further financial accommodation

[68] Resource Management Guide, paragraph 54
[69] Ibid, paragraph 55
[70] Ibid, paragraph 60
[71] Ibid, paragraph 64
[72] Ibid, paragraph 66
[73] Ibid, paragraph 65
[74] Ibid, paragraph 69
[75] Ibid, paragraph 68
[76] Ibid, paragraph 18

was not available and the small business' bank enforced its security over the family home? Would the action by the bank and any financial damage it caused be considered a direct result of the defective administration?

- *necessary and reasonable assumptions as to the amount of compensation:* the Scheme's provisions allow the decision maker considerable scope in determining the amount of compensation. If the interpretation of defective administration is broadened, then a broader assessment of detriment would follow and the decision maker is permitted to make appropriate assumptions, if required, as to the amount of fair and reasonable compensation in the circumstances.

The Review is of the opinion that the Minister or the Commissioner is also in a position, if they chose to do so, to provide guidance about the interpretation of detriment directly resulting from defective administration under the current provisions of the Resource Management Guide.

7.3 Standard of proof

The Resource Management Guide provides that:

> *Documentary or incontrovertible proof of defective administration is not an essential requirement. However, there must be sufficient evidence to enable the decision maker to form the opinion that defective administration has occurred.*[77]

That provision is supported by paragraph 47 of the Guide:

> *Cases may arise where individual instances of administrative omissions or errors may not be regarded as unreasonable when considered in isolation from each other, but may constitute defective administration when considered in totality and in the context of the combined impact of the omissions or errors on the claimant.*

While the ATO can seek further information from the claimant, it is not under any obligation to actively seek out information beyond what the claimant has provided.[78]

The ATO CDDA Manual[79] sets out the process for General Counsel officers to examine ATO documents and obtain business line briefings relevant to a CDDA claim. As a result, General Counsel will have detailed information about the conduct of the ATO officers and whether it complied with the ATO's prescribed processes and procedural requirements.

The investigation can give rise to an obligation to share some of that information with the claimant:

> *If a document relevant to a claim is found by an entity, it cannot be disregarded simply on the basis that it was not provided by the claimant. Procedural fairness requires that the substance of documents (relevant to the claim) held by the entity but not known to the claimant is shared with the claimant*.[80]

[77] Ibid, paragraph 49
[78] Ibid, paragraph 50
[79] Step 2, page 1
[80] Resource Management Guide, paragraph 51

The Resource Management Guide specifies the level of proof required to substantiate a claim:

> *Where evidence of defective administration is limited, an assessment must seek to balance the plausibility of the claimant's account of their actions and the plausibility of the allegations against the entity, as well as other possible explanations, in order to determine what is more likely to have occurred*.[81]

The plausibility test has been included in Finance circulars at least since Circular No 2006/05 *Discretionary Compensation Mechanisms.*[82]

In civil courts, the standard of proof is based on the balance of probabilities and the ATO Manual adopts that standard. It says:

> *The standard of proof for the CDDA Scheme is the civil standard, or the balance of probabilities. This means that a decision maker should consider where (sic) it was 'more probable than not' (more than 50%) that defective administration took place*.[83]

There are two recent Australian Government redress schemes where plausibility was adopted as a lower standard of proof than the civil balance of probabilities.

First, there was the Defence Abuse Response Taskforce which provided redress (including a reparation payment of up to $50,000) in 1,751 claims of physical or sexual abuse in the Australian Defence Force. The Taskforce adopted plausibility as the standard of proof for acceptance of claims. The Taskforce accepted an allegation of abuse as true, if satisfied on all the material available, that it was plausible.[84] This plausibility standard was less than the civil standard as the onus of proving the truth of their allegations on the balance of probabilities would have been an insurmountable obstacle.[85]

Then came the Royal Commission into Institutional Responses to Child Sexual Abuse which adopted a slightly higher standard:

> *We are satisfied that the standard of proof for a redress scheme should be lower than the common law standard of proof. In all of the circumstances, we are satisfied that 'reasonable likelihood' should be the standard of proof adopted for the redress scheme. Although in many cases it may make little difference whether the standard is plausibility or reasonable likelihood, we consider that reasonable likelihood can be applied as a higher standard than plausibility.*[86]

The Review concludes that the civil test of balance of probabilities specified in the General Counsel Manual is not the correct test for CDDA claims. The Review recommends that General Counsel's procedures and the CDDA Manual should be based on the plausibility standard of proof, not balance of probabilities.

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[81] Ibid, paragraph 52
[82] Paragraph 32, page 20
[83] General Counsel CDDA Manual, Key Decision Making Principles, Fact Finding
[84] Defence Abuse Response Taskforce Final Report, arch 2016, page 13
[85] Robert Cornall AO was Chair of the Taskforce from December 2014 to conclusion in 2016 (formerly Deputy Chair from 2012)
[86] *Redress and Civil Litigation Report,* 2015, page 41

7.4 Deeds of release, indemnity and confidentiality

The ATO requires some claimants to sign a deed of release as a precondition to receiving an approved compensation payment. The General Counsel Manual says:

> *In some circumstances, a payment under the CDDA Scheme may be accompanied with a deed. Generally, a deed is used for payments of $2,000; however the individual circumstances of each claimant should be taken into account*.[87]

A number of reviews considered by the Review and several people interviewed disagreed with this practice. The core of their objection appears to be that the confidentiality obligation limits transparency by preventing claimants talking publicly about their matter after it is settled. As a result, it is said to contribute to a lack of transparency and public awareness about the CDDA Scheme.

The Review has carefully considered this objection but supports the continued use of confidentiality agreements in deeds for four reasons:

- other agencies administering CDDA claims take a similar approach and it is consistent with common practice in commercial disputes
- the secrecy provisions of the Tax Administration Act make it difficult to have an informed public discussion about individual claims for compensation
- it is in the interests of all parties to bring a compensation claim to a conclusion and put it behind them, and
- the concerns about lack of transparency and public awareness can be dealt with in other ways which are discussed in Section 8.

Recommendation 3: That the Commissioner give the ATO's CDDA practitioners guidance about the interpretation of defective administration and detriment in CDDA claims made by small business.

Recommendation 4: That, if necessary, the ATO amend its service, conduct or performance standards to support the Commissioner's guidance on the interpretation of defective administration.

Recommendation 5: That the ATO adopt plausibility as the standard of proof in CDDA claims instead of the balance of probabilities.

Recommendation 6: That the Review does not support calls for removal of confidentiality agreements from deeds of release.

[87] Step 5, Outcome 2

SECTION 8: ISSUES FOR SMALL BUSINESS

This Section looks at several issues for small business which were brought to the Review's attention in interviews, submissions and earlier reports and inquiries.

8.1 Communication and transparency

There was consistent support for the view that the CDDA Scheme is not widely known or understood and that includes a lack of awareness within the small business community, tax agents and ATO business lines.

The Review undertook an investigation of the information available through online searches and the case study below describes those enquiries.[88]

Case study 1: Electronic searches for Compensation for Detriment Caused by Defective Administration

Entering 'Compensation for Detriment Caused by Defective Administration' in the search engine immediately brings up the CDDA page on the Department of Finance website. There is a succinct explanation of the Scheme's key features on the opening page and links to specific sections and a printable version of Resource Management Guide No 409.

Previous reviews have been critical of the information available about the CDDA Scheme on the ATO website. Using basic search terms, such as 'ATO compensation', 'financial compensation from the ATO', 'defective administration ATO' or 'ATO maladministration' will go straight to a page headed Applying for Compensation – Australian Taxation Office.

The page itself contains details about legal liability and CDDA claims and links to the CDDA information page on the ATO's website. Some browsers will preview the entire page on the search index so the information is readily accessible without having to click a link. The information about the CDDA Scheme is plainly written, to the point and easy to understand.

Using similar search terms in the search function on the ATO website will also link you to the ATO's CDDA information. While it is clear that the ATO has taken steps to ensure information about CDDA is more accessible, there are some limitations. For example, searching for 'maladministration' using the search function on the ATO's website will not find any information on the CDDA Scheme. While it is different to defective administration, interviewees often referred to 'maladministration' and it would be worth including this search term.

The ATO website's virtual assistant, Alex, cannot assist with searches for the CDDA Scheme. Asking Alex about applying for compensation will not bring up any information about the Scheme.

[88] Results may vary depending on the search engine

The Review concluded that information about compensation and the CDDA Scheme is reasonably available through electronic searches. The availability and accessibility of information about defective administration on the ATO's website appears to be comparable to other government agencies. While some aspects of the ATO's online search function could be improved, it is not hard to find information about the CDDA Scheme online.

However, that information is only available to people who know about the Scheme or are enquiring more broadly about compensation from the Tax Office. The task facing the ATO is to bring the CDDA Scheme to the attention of small business proprietors, tax agents and others who could usefully have knowledge and information about the Scheme and how it works.

This should not be a difficult task for the ATO, using its already established and other potential communication networks including:

- the ATO Small Business website
- creating a link to the ATO's CDDA information on the 'Supporting your small business' page on the ATO website
- regular direct communication to small businesses from the Small Business Division
- direct communication to tax agents
- the Inspector-General of Taxation
- the Australian Small Business and Family Enterprise Ombudsman
- indirect communication to tax agents through their professional associations
- through tax agent continuing professional development programs
- ATO speeches at seminars and conferences, and
- the Law Council of Australia's Taxation Committee.

It is not easy to grasp the concept of defective administration. It will be important to ensure that soft and hard copies of information about the CDDA Scheme are clearly explained in everyday language and supported by de-identified case studies based actual claims that illustrate how the Scheme works.

The case studies should include an explanation of the defective administration, the detriment it caused, the compensation paid and how it was assessed. They should illustrate unsuccessful claims and why they failed: outside the scope of the Scheme, no defective administration or no detriment suffered. The Practical Guide to the ATO Code of Settlement is an excellent example the use of de-identified case studies.

The use of de-identified case studies was supported in submissions. CPA Australia submitted that:

> *Examples of successful claims and further guidance should be published*.[89]

Chartered Accountants Australia and New Zealand criticised the lack of de-identified case studies:

> *In particular, there are no de-identified examples of case studies of situations where compensation has or has not been provided. Knowledge of CDDA outcomes should, in our view, be better shared*.[90]

The Review recommends that the ATO undertake a comprehensive and ongoing communication program to raise awareness about the CDDA Scheme among small businesses, tax professionals and their professional bodies and to assist other organisations and members of the public who want to know about ATO compensation.

8.2 CDDA Scheme assistance for small businesses

The Prime Minister made the following observation in a speech to the Australian Chamber of Commerce and Industry last year:

> *But I understand the concerns … of small business when it comes to dealing with the ATO. There is no denying the complexity involved and we are focused on reducing that complexity. We know you're focused on running your business, not studying the Tax Act or sifting through rules and determinations*.[91]

During the course of the speech, the Prime Minister announced the establishment of a small business concierge service to be run by the Australian Small Business and Family Enterprise Ombudsman. The objective of the concierge service is to provide knowhow about the Administrative Appeals Tribunal's procedures and support throughout an AAT matter.

The ASBFEO website provides this information about the concierge service:

> *Our Assistance Team comprises small business specialists and case managers who respond to requests for assistance from small business taxpayers who have received a negative decision from the ATO. The small business specialists and case managers will provide:*
>
> - *information on the AAT procedures for reviewing a decision*
> - *access to legal advice before and after an application is lodged with the AAT*
> - *access to support including a reduced AAT application fee and fast track processing, and*
> - *ongoing support and assistance until a decision is reached.*

The exact details of the concierge service are not directly relevant to this Review but the concept is.

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[89] Letter dated 15 April 2019
[90] Submission dated 5 April 2018 (sic)
[91] Annual Dinner, 28 November 2018

There are a number of areas where the government provides advocacy or other assistance to citizens seeking access to Commonwealth benefits or entitlements under complex federal legislation. Examples include:

- the National Disability Advocacy Program, and
- the National Aged Care Advocacy Program

The Review considers that a similar program – possibly called the Small Business Compensation Assistance Service – can be justified for small businesses seeking compensation under the CDDA Scheme.

The Review recommends that the Government establish a Small Business Compensation Assistance Service open to all small businesses even if they have a professional adviser assisting them (because some professional advisers have limited knowledge of, or experience with, the CDDA Scheme). The Service would be administered by the ASBFEO and its assistance would include:

- advising small businesses on potential claims for compensation under the CDDA Scheme
- assisting them to complete and lodge an application for compensation and to supply relevant documentation to establish both defective administration and (when required) detriment
- just as important, advising them when they do not have a sound basis for a claim (that is, the claim is outside the scope of the Scheme, there is no defective administration or no detriment)
- providing assistance and advice during the course of the application for compensation
- reviewing the outcome and, if the claim was unsuccessful in whole or in part, the reason why it was not approved, and
- advising about the possibility of an ATO reconsideration or internal review of an adverse decision, and
- advising about the possibility of a complaint to the Inspector-General of Taxation.

While this proposal would come at a modest cost, the following factors should be taken into account:

- it is based on the same justification as the concierge service (the difficulties under-resourced small businesses face in dealing with the ATO and complex tax legislation)
- experience in similar schemes shows that, where there is no sound basis for a compensation claim, advice to that effect from a trusted independent adviser often results in the potential applicant not pursuing the matter further. As a result, there are consequent savings in the scheme's administration costs

- it would facilitate the administration of CDDA claims

- it would address some of the concerns about lack of independence in the CDDA process through the ASBFEO's direct involvement in individual claims, and

- it should be seen by small business as a positive move towards more transparency in the CDDA process, particularly if it is supported by the ATO.

The Review also received a lot of comments about the imbalance of power and resources (money, people, expertise) between the Tax Office and small business and the stress and even fear that can arise when dealing with the ATO. This proposal would go some way to alleviating that concern for small businesses making a CDDA claim.

8.3 Information technology outages and system failures

The Review received submissions about the effect ATO IT outages and system failures can have on tax professionals. Professional bodies submitted that outages and system failures affected their members' ability on occasion to provide timely tax services to clients.

While acknowledging there are no current issues with the ATO's administration of information technology, Chartered Accountants Australia and New Zealand submitted:

> *Increasingly, there is a greater reliance by taxpayers and tax agents on digital interactions with the ATO. When the ATO went through its digital change programme some years ago and later experienced major outages in 2016 and 2017, we understand there were some claims made under the CDDA programme by both taxpayers and tax agents for compensation. Our understanding is that claims made by tax agents were rejected by the ATO on the basis that there was no defective administration and that there was no demonstrable loss. There appears to be a difference between what tax agents and the ATO consider to be defective administration and what can be claimed in compensation.*

The Review notes that the Commissioner acknowledged the effect of the recent disruption and its effect on tax practitioners in his Foreword to the June 2017 *ATO Systems Report* which analysed the causes, impacts and responses to the IT outages in December 2016 and February 2017:

> *We are very mindful of the disruption that the outages caused the community and our key stakeholders – tax practitioners, the superannuation industry and software providers. I apologise again for the inconvenience that has been experienced.*

CPA Australia argued that:

> *The entire CDDA Scheme should explicitly include compensation related to digital systems.*[92]
>
> *Despite the mandatory requirements imposed on practitioners and businesses to utilise ATO systems to lodge and report information, there are no service agreements provided by the ATO which can form the basis of determining whether the administration has been defective. While the ATO is now publishing service commitments and system availability, this falls short of*

[92] Letter 15 April 2019

> *performance agreements such as those used for public transport which entitle eligible users to compensation if service falls below a standard.*[93]

In a meeting with representatives of the Institute of Public Accountants, they identified IT outages and the impact on intermediaries as their main issue.

The Inspector-General expressed a similar view in the November 2018 *Future of the Tax Profession Report.* The IGT was concerned that tax practitioners were left without any compensation payments for ATO system failures and outages due to the restrictive and discretionary nature of the CDDA Scheme. The IGT said:

> *… the CDDA scheme should either be improved or a separate compensation scheme for tax administration be created to include a right of external review of the original compensation decision*.[94]

The IGT recommended that the ATO:

> *… align its service standards for the performance of its systems with those of commercial providers, including a dedicated scheme for compensation where outages or system failures result in a loss for the users*.[95]

The ATO disagreed with that recommendation. It responded:

> *We have approved Target Service Standards … It must be made clear that service standards are aspirational targets and are not a formal agreement between the ATO and the community or tax profession. Where the ATO does not meet its service standards, the ATO has relief provisions to support the community. Examples of these include waivers to penalties or extensions of lodgment dates for returns.*
>
> *With regard to compensation, the community and the tax profession can, through the … CDDA Scheme, seek compensation for situations where they include a loss as a direct result of outages or system failures.*

There are several points to make about that exchange.

First, the CDDA Scheme requires the applicant to establish defective administration before considering what, if any, direct loss resulted from it. Large computer systems are subject to outages from time to time and major system upgrades can cause disruption in the normal course of business. They are not automatically evidence of defective administration.

As the Institute of Public Accountants said in its submission:

> *While ATO systems have since been free from unexpected outages, in this digital age, there is a sense of inevitability that systems are capable of suffering an outage at any point in time.*[96]

[93] Submission, page 2
[94] Report, paragraph 4.159
[95] Recommendation 4.2 g
[96] Submission, page 5

Second, the ATO operates a complex computing platform managed by a combination of ATO staff with IT expertise and contracted service providers. The actions of contracted providers are not covered by the CDDA Scheme.[97]

Third, the Commissioner refers to the relationship between the ATO and tax professionals as a partnership but the ATO bears the cost of increasing digital efficiency in the tax system.[98] It is not a commercial arrangement where tax professionals pay for a service. The IGT found:

> *Relevantly, over the three financial years from 2014-15 to 2016-17, the expenditure on platforms for tax practitioners, such as the ATO Portals and PLS[99], has exceeded those for self-service channels ($39,491,980 compared to $33,708,590).*[100]

There may be circumstances where some claims for IT outages and systems failures fall within the scope of the CDDA Scheme and in those cases compensation will be available. However:

- consideration of changes to the CDDA Scheme is a matter for the Minister for Finance, and
- consideration of the establishment of a dedicated compensation scheme for tax administration which includes outages and system failures as proposed by the Inspector-General is a matter for Government.

8.4 The time and cost involved in dealing with the ATO

It is widely acknowledged that tax law is complex and compliance can involve time and cost which a small business taxpayer often can ill afford. While compliance procedures may significantly disrupt a small business, there will not be any basis for a CDDA claim unless there is defective administration and detriment resulting directly from it.

Reviews and audits can be triggered automatically by the ATO's computer systems based on an analysis of information in returns lodged by the taxpayer. Compliance procedures can go on for a long time but that does not necessarily mean there has been defective administration even if the review or audit finds nothing of concern.

Alternatively, the ATO's inquiries could result in new tax assessments and possibly penalties that could lead to an objection. The objection officer may uphold or dismiss the objection or make a finding that gives some result to both the ATO and the objector. Even if a taxpayer is 100% successful, the taxpayer bears the costs of the objection.

The following case study illustrates how the automatic triggering of reviews and audits can result in compliance processes that take more than a year and tens of thousands of dollars in costs for the taxpayer. However, the actions taken by the ATO did not amount to defective administration as they were undertaken in accordance with the appropriate processes.

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[97] Resource Management Guide, paragraph 16

[98] For example, in 2017-8 the ATO transitioned all tax return types to the Practitioner Lodgement Service which is on a new, interactive Standard Business Reporting platform with a wider range of interactive services for tax and BAS agents through their practice management software: Annual Report 2017-18, Commissioner's Review, page 2

[99] Practitioner Lodgement Service

[100] *Future of the Tax Profession Report*, paragraph 4.165

The issue of compliance cost for small business is discussed further in Section 9.

Case study 2: The time and cost involved in ATO compliance

A claimant alleged their business had incurred detriment (large refinancing and legal costs) as a result of delay in the payment of a Research and Development rebate and the time it took to finalise multiple GST audits and a subsequent objection.

After the claimant lodged income tax returns, the ATO's systems triggered an R&D review that resulted in the claimant's R&D credit being retained. The claimant maintained that, as a result of the retention of the R&D credit and the time it took to finalise the R&D review, the business was forced to borrow money and rely on loans to maintain the company's solvency.

The CDDA decision maker concluded the R&D review was conducted in accordance with service standards and was in fact completed early. Further, based on information provided during that review, the claimant lodged a voluntary disclosure that ultimately reduced the amount of the R&D credit.

Shortly after the R&D review had been finalised, the ATO systems automatically triggered audits relating to the claimant's Business Activity Statement reporting, specifically concerning claimed GST refunds. On commencement of the audits, unpaid GST credit amounts were retained by the ATO. The claimant alleged the ATO was unfairly targeting their business and that the delay in finalising the audits contributed to the loss claimed.

The CDDA investigation found that the GST audits were conducted in accordance with ATO service standards and that the time taken to complete them was justifiable as the audit outcomes were dependent on analysis of information provided by the claimant and other parties. ATO General Counsel concluded it was appropriate and reasonable to undertake the BAS audits and there was no evidence of defective administration in their execution.

With legal assistance, the claimant lodged objections to the final audit decisions and to amended income tax assessments. The claimant also provided further substantiation material. The decision maker disallowed the objections raised by the claimant in relation to the previous audit and review actions, except for the most recent periods. As a result, the claimant was entitled to some further R&D and GST credits.

The objection decision was to disallow the objections in relation to the majority of the disputed BAS and income tax assessments. The minority objection decision to allow additional GST credits and R&D tax offsets hinged on material that only came into existence after the earlier audits had commenced.

The decision maker found that there was no defective administration and therefore no compensation was payable under the CDDA Scheme.

Recommendation 7: That the ATO undertake a comprehensive and ongoing communication program to raise awareness about the CDDA Scheme among small businesses, tax professionals and their professional bodies and to assist other organisations and members of the public who want to know about ATO compensation.

Recommendation 8: That the Government establish a Small Business Compensation Assistance Service open to all small businesses to be administered by the Australian Small Business and Family Enterprise Ombudsman.

SECTION 9: ANALYSIS

In 2017-18, the Australian Tax Office's net tax collections were almost $397 billion and its compensation payments under the CDDA Scheme totalled $409,035. In the ATO big picture, the Scheme would appear to be of little importance but the opposite is the case. A quick glance at the Key CDDA Reviews and Milestones listed in Appendix 2 illustrates the point.

The Scheme was founded on the core principle that government agencies have a moral obligation in the defined circumstances to make good the damage they cause although now the obligation is expressed in terms of fairness and equity.

Since 1995, the CDDA Scheme – and the ATO's administration of it – has been the subject of, or included in, reviews, inquiries and reports by parliamentary committees, the Ombudsman, the Inspector-General of Taxation, the Australian National Audit Office, the Department of Finance, the Treasury, the Administrative Review Council and the media.

The reason for this ongoing interest is that, for taxpayers aggrieved by their dealings with the ATO, the CDDA Scheme may offer the only prospect of a discretionary compensation payment.

This Section analyses some of the factors that have to be taken into account in assessing the Scheme's effectiveness.

9.1 The location of the CDDA function

The Office of General Counsel is part of the ATO's Enterprise Strategy and Corporate Operations Group. General Counsel lawyers handling CDDA claims also deal with freedom of information and employment matters. General Counsel's remit includes a broader range of non-tax related matters (legal advice, commercial law and civil claims that do not relate to a tax dispute).[101]

Over the last few years, there have been calls from the House of Representatives Standing Committee on Tax and Revenue and the Inspector-General of Taxation for the Government to create a separate appeals group in the ATO under a (fourth) Second Commissioner. The group would be responsible for managing tax disputes for all taxpayers, including pre-assessment reviews; objections; litigation including identifying test cases and providing oversight on settlements; and facilitating the use of ADR throughout the compliance and dispute resolution process.

During that period, the Commissioner endorsed the creation of an administrative review function that would sit under a (third) Second Commissioner independent of the ATO's audit function. That function is vested in the Law Design and Practice Group under Second Commissioner Andrew Mills.

The Second Commissioner has said:

[101] Practice Statement Law Administration PS LA 2009/9

> *The RDR [Review and Dispute Resolution] approach is based on a philosophy that fair, impartial and independent dispute resolution and prevention services should be accessible to all taxpayers.*
>
> *Since 2015 there has been a particular focus on promoting a culture of fairness and greater consideration of each client's circumstances in dispute resolution as an aim and outcome of resolving a dispute. Previously, staff had focused on meeting a measurement that was a time-based KPI, resulting in work management practices that didn't necessarily account for a good experience for taxpayers.*
>
> *The fairness mindset is promoted from both the perspectives of procedure and outcome with Review Officers*.[102]

General Counsel officers have told the Review they have informal interactions with Review and Dispute Resolution when appropriate and have utilised their dispute resolution assistance.

The Review considers there is a good case for moving CDDA claims[103] from the Office of General Counsel to the Law Design and Practice Group. This suggestion is not a criticism of General Counsel. It is based on the view that the CDDA function would benefit from being located with the ATO's independent dispute resolution area.

While CDDA claims are not standard disputes, they are claims for financial compensation that require similar skills and an understanding of both ATO procedure and the cultural mindset the Commissioner wants the organisation to adopt in its dealings with taxpayers.

The relocation of the CDDA function could result in:

- synergies obtained from association with a group focused solely on dispute resolution
- earlier identification of potential CDDA claims through regular interaction within the Law Design and Practice Group
- the creation of effective feedback loops between the CDDA, dispute resolution and audit functions within the ATO, and
- development of red flags from the CDDA claimants' experience to prevent a recurrence of similar claims in future.

It is interesting to note that, when the CDDA Scheme was established, it was thought that requiring agencies to manage their CDDA claims and pay compensation from their own budget appropriation could lead to process improvements. The 1995 Cabinet submission 2207 said:

> *One potential, but unquantifiable, benefit is the incentive Agencies would have to continually strive for improvements in their administrative efficiency and effectiveness*.[104]

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[102] *Tax in a changing world – change is the new black,* Australasian Tax Teachers Association Annual Conference, 17 January 2019

[103] Including assistance with Act of Grace claims

[104] Paragraph 18

9.2 Various forms of ATO redress

There are various ways ATO errors or omissions can be dealt with and the CDDA Scheme is the remedy of last resort (other than Act of Grace in special circumstances). Acting within its statutory powers, the ATO can amend assessments or they can be amended or overturned by a successful objection or AAT or court action. Penalties can be withdrawn, extra time allowed for compliance and debt repayment agreements arranged.

However, a taxpayer cannot claim reimbursement of costs incurred in its dealings with the ATO (say, a successful objection) as the Parliament has not enacted any provision authorising their payment.

In any event, overturning a decision on review does not necessarily mean the initial decision was wrong. Some matters call for judgment and reasonable minds can differ as can be most readily seen in judicial decisions overturned on appeal to a higher court. In regard to administrative decisions, the President of the AAT has explained the Tribunal's role is to review government decisions on their merits:

> *This important task requires us to stand in the shoes of the original decision maker and remake the decision. In most cases, we have new or additional information that was not available to the original decision maker. Having regard to all the facts and circumstances of a case, the Tribunal must reach the correct decision according to the law. In cases where there is a discretion, we must make the preferable decision, not on the basis of personal preference, but taking into account factors set out in the law and relevant policy*.[105]

A taxpayer cannot sue the ATO for damage caused by negligence in the discharge of its duties. In *Harris v Deputy Commissioner of Taxation*, Justice Grove said:

> *There is no identified duty of care specified as being owed by the [Tax Office] to the plaintiff. Such a duty is not established by reference to proclamations such as the Taxpayers' Charter which express aims of treating citizens from whom tax is to be levied, fairly and reasonably. Even if there was a departure from some standard specified in such a document, it could not vest a private right to recover tort damages in a person affected by the departure. … There is no basis upon which to conclude that there is a tort liability in the Australian Taxation Office or its named officers towards a taxpayer arising out of the lawful exercise of functions under the Income Tax Assessment Act*.[106]

9.3 Getting it right

The Government and the ATO recognise the Tax Office has a responsibility to make it as easy as possible for small businesses to understand and correctly meet their tax obligations. There are too many initiatives to assist small business to list here but some recent examples include: the appointment of an Australian Small Business and Family Enterprise Ombudsman; the establishment of a Small Business Division in the AAT and an accompanying concierge service; and the expansion of the tax clinics program.

The ATO continues to make improvements to its structure and administrative procedures that will benefit small businesses. Examples include: the appointment of a Second Commissioner, Law Design and

[105] AAT Annual Report 2016-17, page 2
[106] (2001) 47 ATR 406 at 408, Grove J

Practice Group; establishing a Small Business Division under and a Small Business Deputy Commissioner; enhanced Review and Dispute Resolution and inhouse facilitation and mediation processes; introduction of Dispute Assist to guide unrepresented taxpayers through the system; the publication of the *Cash Flow Coaching Kit;* and the Small Business Newsroom newsletter providing tax and superannuation updates.

Nonetheless, tax law is complex and compliance can be complicated so it is inevitable that both small business taxpayers and the ATO will make mistakes.

9.4 Disproportionate impact on small business

The ATO conducts surveys to monitor whether taxpayers feel they are fairly treated by the Tax Office and those surveys have had encouraging results.

However, citizens are expected to know the law (despite the complexity of tax law) and the ATO has statutory responsibility to administer the Tax Administration Act and collect tax for the benefit of the Australian economy and the community at large. As a result, mistakes can be made and disagreements will arise between the ATO and small businesses.

The ATO's reviews and audits and any subsequent objections and appeals cost time and money which fall entirely on taxpayers (no matter what the outcome) because the Act does not make any provision for reimbursement and the CDDA Scheme will be of no assistance unless there was defective administration.

The net result is that the ATO's standard compliance procedures can have a disproportionate impact on a small business mainly due to the lost time involved and because the costs involved are disproportionately large. The financial fragility of many small businesses is clearly exposed in Appendix 3 and small business proprietors can suffer stress, anxiety, mental health and other personal issues.

This disproportionate impact occurs between small businesses as well. A sole trader will bear the whole cost of an ATO audit whereas a three person business can spread the cost over all the partners.

The Review is not suggesting that compliance costs should be reimbursed. It is noting that this disproportionate impact is, in its view, at the heart of small business concerns with the ATO. It also provides one explanation for the continuing Government and public interest in the CDDA Scheme.

So the question is: what can be done to mitigate the disproportionate impact?

The Review took particular notice of Mr Mills' comment about 'promoting a culture of fairness and greater consideration of each client's circumstances'.

A partial solution may lie in the ATO taking small business taxpayers' individual circumstances more into account in its dealing with them. In this regard, the Review noted Practice Statement Law Administration PS LA 2011/18 with interest. Prior to issuing a garnishee notice, it requires the Commissioner to have regard to:

> *… 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*.[107]

[107] Paragraph 108

The Commissioner could consider the practicality of including an appropriately worded requirement in the ATO's prescribed procedures specifying that a small business' financial and personal capacity to respond to a review or audit is a factor to be taken into account by ATO officers in discharging their duties.

Depending on the precise formulation and the individual circumstances, failing to comply with that requirement could fall within the definition of defective administration. A provision of this nature could potentially alleviate some of the disproportionate impact the ATO's procedures can have on small business.

Some guidance may be found in the Commonwealth's *Legal Services Directions 2017* that regulate the way the Australian Government conducts litigation. Government agencies are required to act as a model litigant which includes the following obligations[108]:

- dealing with claims promptly and not causing unnecessary delay
- making an early assessment of the prospects of success or liability
- endeavouring to avoid, prevent and limit the scope of legal proceedings wherever possible
- keeping the costs of litigation to a minimum
- not taking advantage of a litigant who lacks the resources to litigate a legitimate claim[109]
- not taking technical defences, and
- factoring in the costs of continuing to defend or pursue a claim.

The ATO could consider formulating directions for the conduct of small business audits and reviews aimed at expediting the process, taking a risk based approach to minor discrepancies and minimising the compliance cost for the taxpayer.

9.5 Is the CDDA Scheme fit for the ATO's purpose?

The adverse perceptions of the CDDA Scheme identified throughout this Report and its limited use over the last five years indicate the Scheme is not working effectively for taxpayers in their dealings with the ATO. For the last 20 years, the reviews and reports listed in Appendix 2 have consistently raised concerns about the Scheme and suggested improvements. Some concerns arise from the inherent limitations of the Scheme. Others involve the ATO's procedures and implementation.

There have also been recommendations to introduce a new compensation scheme for taxpayers in their dealings with the ATO. However the perceived problems with the CDDA Scheme may also be problems for any alternative compensation arrangements.

[108] See Legal Services Directions 2017, Appendix B

[109] Paragraph 70 of the Resource Management Guide has a similar intent – the ATO is not to take advantage of its relative position of strength

The CDDA Scheme was designed to allow flexibility in its application to the particular circumstances of an individual agency. The Review suggests the ATO take the opportunity to reassess its administration of the Scheme as suggested in this Report. If the recommendations in this Report lead to measurable improvements, the Review considers that the CDDA Scheme may achieve its intended purpose – that is, to compensate for detriment directly resulting from the ATO's defective administration.

However, if taxpayers have higher expectations of compensation or redress for small business, then the CDDA Scheme will not meet them and was not meant to do so.

9.6 Future direction

The Review suggests that the Commissioner, in consultation with the Minister, should decide what the ATO wants from the CDDA Scheme and how it can be achieved. That strategic objective should be widely disseminated within the ATO and more broadly. The Review proposes the responsibility for implementing a strategic plan to reach the ATO's goal should be vested in the Second Commissioner, Law Design and Practice.

If there is a cost involved in making the Scheme more effective, it should be assessed against the benefits:

- small business taxpayers will derive from a CDDA Scheme that may better meet their needs, and
- for the ATO in addressing at least some of the adverse perceptions small business and others hold currently hold about the ATO's CDDA Scheme.

The effectiveness of the recommendations proposed in this Review should be monitored by the Second Commissioner, Law Design and Practice. The Review suggests the Second Commissioner should make annual progress reports to the Minister and the Commissioner. In 2022-23, a thorough evaluation should be undertaken and, if the outcomes have not met expectations, further changes to the CDDA Scheme as implemented by the ATO or other alternatives should be considered.

Recommendation 9: That the CDDA function be moved from the ATO Corporate business line to the Law Design and Practice Group.

Recommendation 10: That the Commissioner consider the practicality of including an appropriately worded requirement in the ATO's prescribed procedures specifying that a small business' financial and personal capacity to respond to a review or audit is a factor to be taken into account by ATO officers in discharging their duties.

Recommendation 11: That, in consultation with the Minister, the Commissioner sets a strategic objective for the ATO's use of the CDDA Scheme and vests the responsibility for developing and implementing an implantation plan to reach the ATO's goal in the Second Commissioner, Law Design and Practice.

Recommendation 12: That the implementation of these recommendations be monitored by the Second Commissioner, Law Design and Practice and annual progress reports made to the Minister and the Secretary with a thorough evaluation of outcomes in 2022-23.

SECTION 10: CONCLUSION

The Review has undertaken a detailed enquiry into the history of the Compensation for Detriment Caused by Defective Administration Scheme. It has considered the large number of reviews and inquiries listed in Appendix 2 and lot of other information and commentary as well.

There have been too many suggestions for changes to the CDDA Scheme and the ATO's administration of it to mention them all here. Suffice to say, the Review has carefully considered all of the proposals that came to its attention. Some of them have been adopted or dealt with in a different way that the Review hopes meets the same objective. Some did not fit with the general direction of the recommendations set out in this Report. Others were put aside as they fall outside the terms of reference.

In summary, the Review is of the opinion that the CDDA Scheme can meet the reasonable expectations of small business and the ATO but its effectiveness will be improved by the recommendations made in this Report. Some small business expectations are outside the scope of a discretionary scheme addressing a moral or fairness obligation to compensate for an agency's defective administration.

In making that assessment, the Review has found that a major concern of small businesses is not about defective administration. It is about the disproportionate impact the Taxation Administration Act's strict provisions and the ATO's powers of administration and enforcement can have on them. The remedy to that issue – if there is one – lies outside this scope of this Review.

The Review has been greatly assisted by the advice provided in consultations and submissions received. ATO officers (including in particular senior lawyers in the Office of General Counsel) have cooperated willingly and responded in detail to the many questions directed to them. The Department of Finance's Risk and Claims Branch has provided timely and competent administrative support.

The Review records its appreciation of their input and assistance.

Kerrie-Anne Luscombe, Consultant, and Annabell Shaw, Executive Adviser, participated in and made valuable contributions throughout the conduct of the Review.



Robert Cornall AO

14 June 2019

APPENDIX 1

GOVERNMENT

- Department of Finance, Andrew Jaggers (Deputy Secretary Commercial and Government Services), Nick Hunt (First Assistant Secretary, Procurement and Insurance Division)
- The Treasury, Nick Westerink (Assistant Commissioner ATO), Michael Buscema (Analyst)
- Department of Human Services, Tim Ffrench (Acting Chief Counsel) and Elise Poiner (General Counsel of Commercial Law and Customer Compensation)
- Department of Home Affairs, Lisa Keeling (Assistant Secretary Civil, Commercial and Employment Law Branch in Legal Division)
- Australian Government Solicitor, Matthew Blunn, Leo Hardiman
- Australian National Audit Office, Grant Hehir (Auditor-General), Rona Mellor (Deputy Auditor-General)
- Office of the Commonwealth Ombudsman, Paul Pfitzner (Senior Assistant Ombudsman)
- Australian Small Business and Family Enterprise Ombudsman, Kate Carnell (Ombudsman), Craig Latham (Deputy Ombudsman)
- Acting Inspector-General of Taxation, Andrew McLoughlin
- Deputy Inspector General, David Pengilley
- Office of the Minister for Finance

AUSTRALIAN TAXATION OFFICE

- Commissioner of Taxation, Chris Jordan AO
- Second Commissioner Client Engagement Group, Jeremy Hirschhorn
- Second Commissioner Law Design and Practice, Andrew Mills
- Chief Operating Officer, Jacqui Curtis
- Chief Tax Counsel, Peter Walmsley
- Deputy Commissioner Service Operations, Alex Adams
- Deputy Commissioner Integrated Compliance Line, Will Day
- Deputy Commissioner Review and Dispute Resolution, Jeremy Geale
- Deputy Commissioner Small Business, Deborah Jenkins
- Deputy Commissioner Individuals and Intermediaries, Alison Lendon
- Deputy Commissioner ATO Corporate, Sue Sinclair
- Assistant Commissioner Review and Dispute Resolution, Damien Browne
- Assistant Commissioner External Engagement and Governance, Michelle Rak
- ATO General Counsel Corporate, Jonathan Todd

ORGANISATIONS AND OTHER AGENCIES

- Commercial Asset Finance Brokers Association
- Council of Small Business of Australia CEO, Peter Strong
- CPA Australia
- Institute of Public Accountants General Manager, Tony Greco

- Law Council of Australia, Clint Harding
- Self Employed Australia CEO, Ken Phillips
- Small Business Association of Australia
- The Tax Institute
- Office of the NSW Small Business Commissioner
- QLD Small Business Champion, Maree Adshead
- South Australian Small Business Commissioner, John Chapman
- Victorian Small Business Commissioner, Judy O'Connell

INDIVIDUALS

- Former Inspector-General of Taxation, Ali Noroozi
- Helen Petaia

APPENDIX 2

KEY CDDA REVIEW AND MILESTONES

- **1995:** Cabinet decision devolved CDDA from the Act of Grace Scheme
- **1999:** Ombudsman Own motion investigation: 'To compensate or not to compensate?'
- **2001:** Finance Circular 2001/01: Commonwealth Compensation 'Schemes', Debt Waiver and Write-Offs, Attachment B (CDDA Guidelines)
- **2004:** ANAO (Audit Report No 35, 2003-04: Compensation Payments and Debt Relief in Special Circumstances).
- **2004/5:** Finance in-house review (survey) of CDDA in response to ANAO Report
- **2006**: Finance Circular 2006/05: Discretionary Compensation Mechanisms, Attachment A (CDDA Scheme Guidelines)
- **2009**: Ombudsman Review: 'Putting things right: compensating for defective administration'
- **2009:** Ombudsman Report: 'Executive Schemes'
- **2009**: Finance Circular 2009/09: Discretionary Compensation and Waiver of Debt Mechanisms, Attachment A (CDDA Scheme Guidelines)
- **December 2010:** Senate Standing Committee on Legal and Constitutional Affairs 'Review of government compensation payments'
- **December 2010:** IGT Review into the ATO's Change Program
- **2011:** Confidential Department of Finance Review (survey) of agencies' use of the CDDA Scheme
- **September 2012:** Administrative Review Council – Federal Judicial Review in Australia
- **2014:** Department of Finance Resource Management Guide No. 409: Scheme for Compensation for Detriment Caused by Defective Administration
- **May 2015:** Tax complaints function was transferred to the Inspector-General of Taxation
- **December 2016**: IGT Review into the Taxpayer's Charter and Taxpayer Protections
- **May 2017:** Department of Finance Resource Management Guide No. 409: Scheme for Compensation for Detriment Caused by Defective Administration - update
- **December 2017:** The House of Representatives Standing Committee on Tax and Revenue Inquiry into the 2017 Annual Report of the ATO. Report handed down in February 2019
- **April 2018**: ABC Four Corners program 'Mongrel bunch of bastards'

- **May 2018:** Treasury Review into Small Business Dealings with the Australian Taxation Office (including the IGT submission to the Review)
- **April 2019:** IGT Review into the Future of the Tax Profession
- **April 2019**: Australian Small Business and Family Enterprise Ombudsman Review into the ATO's enforcement of debt recovery
- **November 2018:** Department of Finance Resource Management Guide No. 409: Scheme for Compensation for Detriment Caused by Defective Administration - update
- **2019:** An Independent Review into the CDDA Scheme in relation to the ATO and Small Business (Department of Finance), Robert Cornall AO

Australian Government
Australian Taxation Office

Small business by the numbers

Small business makes a significant contribution to the Australian economy

Small Business are the largest Australian employer category

In 2016/2017 Small Businesses contributed more than $380 billion to the Australian economy#

Data in this document (unless otherwise stated) has been sourced from the Small Business Client Experience Population, which is defined as:

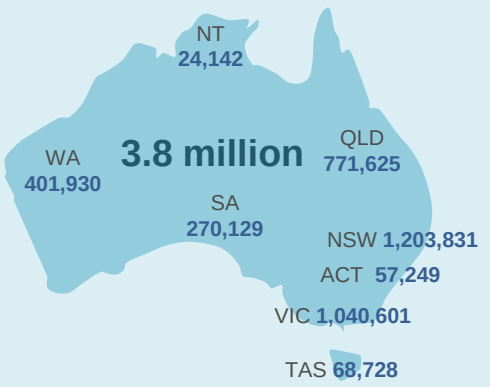
An entity with an Income Tax (IT) or Activity Statement return in the last 3 years, with greater than zero and less than $10 million business expenses or income
But excluding:

- *Entities in Public Groups and Internationals population*
- *Individuals without business income*
- *High Wealth Individuals and Wealthy Australians*
- *Superannuation Funds*

#There is no consistently used definition of Small Business across Government. The Reserve Bank of Australia, the ASBFEO and Fair Work Australia use the ABS definition - based on the number of employees (less than 20 employees)

The small business population

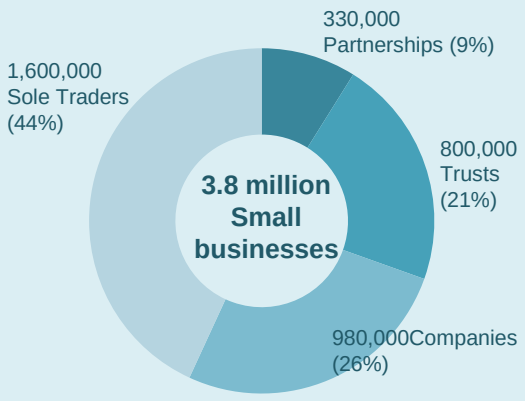
Australia has 3.8 million small businesses that are located in every community across the country^



The concentration of small businesses correlates with the distribution of the general population

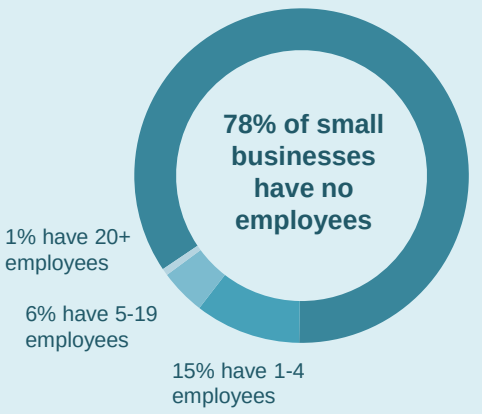
Structure, employees, tax paid

Business structures – the majority of Small Business structures are Sole Traders



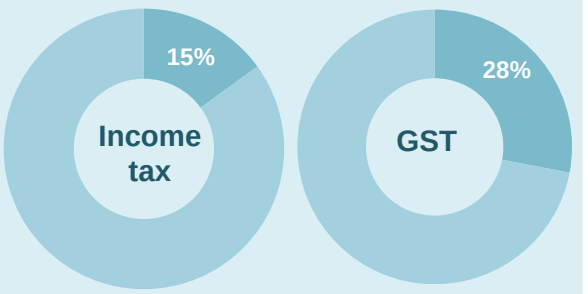
The Small Business Client Experience Population is defined by the following rules: An entity with an Income Tax or Activity Statement return in the last 3 years, with greater than $0 and less than $10m business expenses or income

Small businesses employ around 5.2 million employees^



56% of small businesses that have employees use a company structure

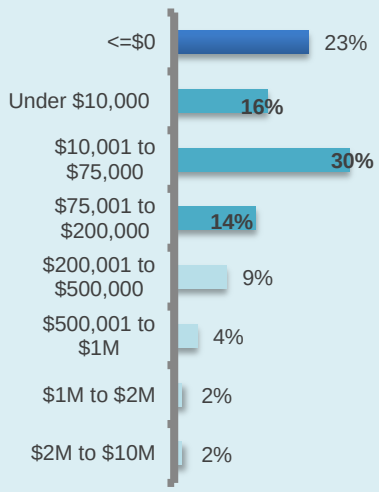
Small business contribute 15% of total income tax and 28% of total GST collected by the ATO



- Income tax includes Fringe benefits tax
- Small business contributions to Excise (including WET) is negligible on a whole of population analysis (2016/17 data)

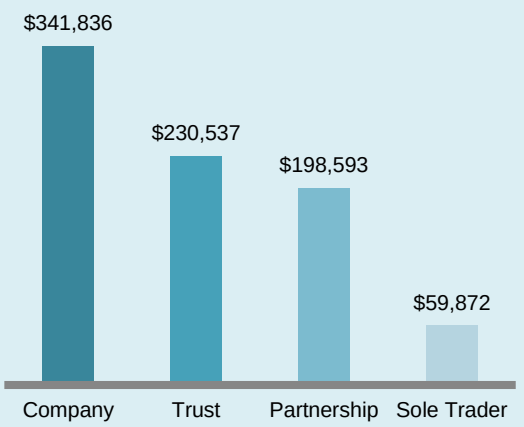
Scale and maturity

Turnover: there are many small players^



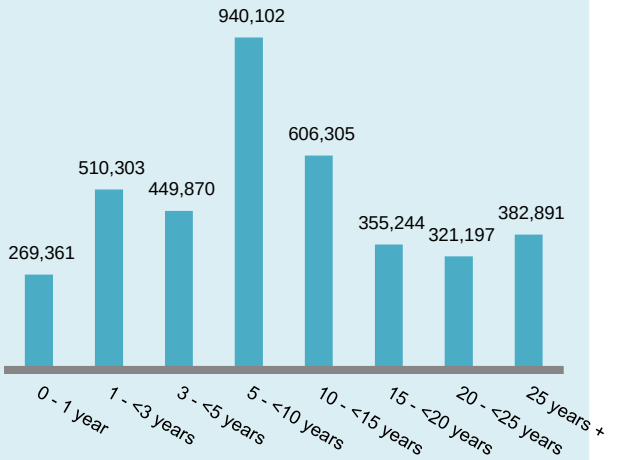
69% of small businesses have a turnover less than $75,000

Average annual turnover by entity type^



Companies and trusts have the highest average turnover. The average turnover for sole traders is **$59,872**

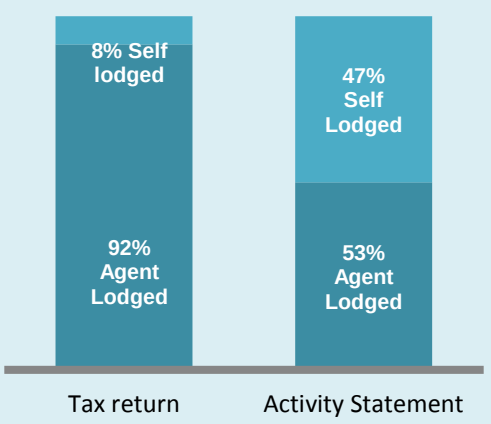
Length of time in business (count)^



57% of small businesses are **less than 10 years old**

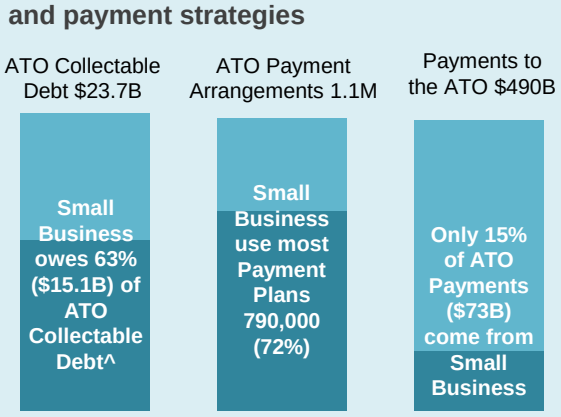
Debt, payment and lodgment

Lodgment channels



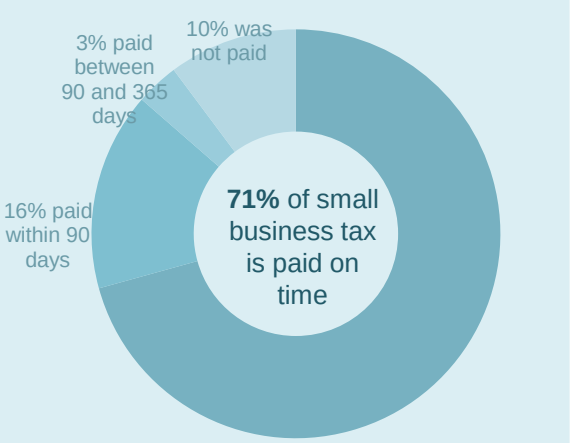
92% use an agent to lodge their Income tax return, but only 53% use their Agent to lodge BAS or IAS (2016/17 data)

Small business is a key focus of our debt and payment strategies



26% ($3.9B) of Small Business collectable debt is under Payment Arrangement
In addition to the $15.1B of Small Business collectable debt, there is a further $1B of disputed debt^

While Small Business debt is large, *most* small business owners pay their tax on time



87.2% of privately owned and wealthy groups pay on time
95.5% of publicly listed business pay on time

Most data is current as at 30 June 2018 – ^Data as at 5 September 2018

Updated September 2018