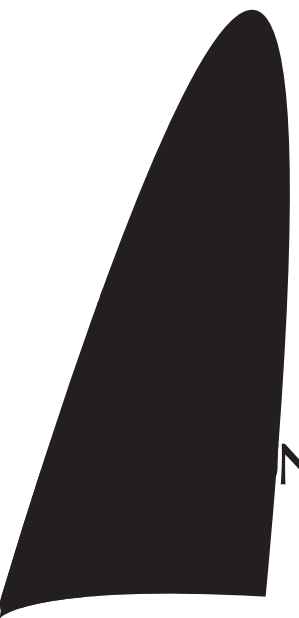


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Australian business taxpayer rights to compensation for loss caused by tax official wrongs – a call for legislative clarification

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Abstract

Australian business taxpayers seeking compensation for losses caused by the wrongs of tax officials have a number of judicially-enforceable and non-judicial avenues of relief. This article outlines each of these options and assesses the suitability and effectiveness of each for resolving compensation claims of business taxpayers. This examination reveals that there are no broadly applicable judicial avenues of relief with any realistic prospects for recovery available to assist Australian business taxpayers. Business taxpayers must turn to non-judicial avenues for recovering compensation from the Commissioner of Taxation. This article contends that these non-judicial avenues of relief are ill-suited for resolving many business compensation claims. Consequently, unlike other taxpayers, Australian business taxpayers often will have no compensation for loss caused by the wrongs of tax officials.

¹ Taxpayer rights to monetary compensation from tax officials derive from a patchwork of judicial and non-judicial discretionary avenues of relief. This article contends that this patchwork of remedies especially disadvantages business taxpayers. It recommends the enactment of legislation to address this situation by clarifying business taxpayer rights to compensation for loss caused by tax official wrongs.

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¹ A broad interpretation of the meaning of 'wrong' is adopted in this article. For the purposes of this article, the term encompasses not just tortious wrongs but any activity causing loss to business taxpayers which is not legislatively sanctioned. Legislatively sanctioned losses would obviously include the collection of taxes by the Commissioner in accordance with the law. While statutory damages are available for particular wrongs such as breaches of the privacy principles in the Privacy Act 1988 (Cth), there are no broad-based Australian statutory remedies.

² The author made broader similar recommendations in John Bevacqua, *Taxpayers' Right to Compensation for Tax Office Mistakes* (2011).

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2.1 Recovering Compensation in Tort

To date, no business or individual taxpayer has succeeded in recovering compensation from the Commissioner in any reported Australian tort case. In fact, very few attempts have been made to pursue the Commissioner in judicial proceedings. Some writers have speculated that this is because '[t]he ATO often rejects such legal claims, where negligence and subsequent financial loss to the taxpayer are clear from the facts, and pays compensation.⁴ However, the principles that have emerged from judicial consideration in these cases suggest that the Commissioner has little to fear in any compensation claims involving allegations of breaches of tortious duties.

For example, in cases where allegations of negligence or breach of statutory duty have been judicially considered, the uniform result has been summary dismissal. The comments of Grove J in *Harris v Deputy Commissioner of Taxation* ('Harris'), which involved a negligence claim against the Commissioner by the operator of a horse-breeding business, are typical of the full extent of the treatment. In that case His Honour stated:

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.⁶

In arriving at this conclusion, Grove J in *Harris* did not apply any of the usual common law tools or principles for determining questions of tortious duties of care applied in cases where public authority tortious liability is in question.

In *Lucas v O'Reilly*⁸ ('Lucas'), Young CJ dealt similarly expediently with an argument by a partner of a share trading business who alleged, among a number of causes of action, a breach of statutory duty by the Commissioner in respect of a foreshadowed (and, the taxpayer argued, erroneous) Notice of Assessment of his tax liability. His Honour stated:

If the cause of action relied upon by the plaintiff is based upon a breach of statutory duty, the plaintiff must show not only that the duty which is alleged

⁴ Duncan Bentley, 'The Taxpayers' Charter: More than a Mission Statement' (1995) 4 *Taxation in Australia* Red Edition 259, 261.

⁵ (2001) 47 *ATR* 406.

⁶ *Ibid*, 408.

⁷ His Honour only makes passing reference to the duty of care in *Harris*.

to have been or to be about to be broken is a duty owed to him but also that the statute creating the duty confers upon him a right of action in respect of any breach... However, it is, I think, clear that the defendant owes the plaintiff no such duty. The duty of the Commissioner is owed to the Crown.

Even torts specifically aimed at compensating citizens wronged by public officials such as the tort of misfeasance in public office¹⁰ have not resulted in a single dollar of compensation to any Australian business to date. Misfeasance in public office allegations against the Commissioner usually fall at the hurdle of demonstrating that a tax official has acted with malice directed toward the taxpayer.¹¹ The difficulties of demonstrating the lack of good faith necessary to prove malice where tax officers are concerned were highlighted by Hill, Dowsett and Hely JJ in *Kordan Pty Ltd v Federal Commissioner of Taxation*¹², a case involving the treatment of trading stock and business losses by the taxpayer: strn75(h)11(e)-w T* [(Tc -0t)6(r)9(nd)6(r)9(nd (co)-) (da9.3

a significant practical impediment to the ability of business taxpayers to recover compensation via this tort.¹⁴

The door has been left open for misfeasance claims against the Commissioner by cases such as *Lucas*¹⁵ and, more recently, the High Court decision in *Commissioner of Taxation v Futuris Corporation Ltd*¹⁶ ('Futuris'). It was observed in *Futuris* that s175 of the ITAA36 would not protect the Commissioner from a challenge to a Notice of Assessment on the basis of an ATO officer having committed a misfeasance in public office.¹⁷ This pronouncement, however, does not change the principles applied in misfeasance cases. Accordingly, it does little to advance the practical prospects of business taxpayer victims of the Commissioner's wrongdoing recovering compensation via a tortious action.

2.2 Recovering Compensation for Breach of Contract

No cases involving allegations of contractual breach arising out of the usual taxpayer interactions with the Commissioner have proceeded to judicial determination. It is generally accepted, however, that the Commissioner owes no contractual duties to taxpayers in carrying out his normal tax administration activities. Isaacs J in his 1926 judgment in *Moreau v FCIT*¹⁸ perhaps came the closest to imposing such duties on the Commissioner, asserting that the Commissioner's function was '...to administer the er18

Act with solicitude for the Public Treasury and with fairness to the taxpayers¹⁹ (emphasis added). However, even Isaacs J stopped ~~short of~~ suggesting any implied contractual duty to treat taxpayers fairly. In any event, such comments have received little judicial attention in Australia.²⁰ The prevailing view remains akin to that expressed in the tortious cases discussed above; that the Commissioner's duties are owed exclusively to the Crown. There seems to be little room in this approach for implied contractual duties of fairness or otherwise -

injunctive goal of estoppel, there is ample opportunity for monetary compensation to be awarded to a plaintiff.²⁶ Accordingly, monetary recompense for expenditure incurred has been awarded in some estoppel claims.²⁷

Again, though, there has been no successful taxpayer claim for compensation in any equitable estoppel action against the Commissioner. In fact, irrespective of the remedy sought, estoppel is a difficult action to make out against the Commissioner. The prevailing judicial stance was bluntly and concisely stated by Kitto J in *Federal Commissioner of Taxation v Wada*²⁸ a case involving a dairy farm business and the treatment of cattle as trading stock:

No conduct on the part of the Commissioner could operate as an estoppel against the operation of the Act.²⁹

More recently, in *AGC (Investments) Ltd v FC*³⁰ a claim relating to tax assessment of the plaintiff's insurance business activities, Hill J expressed similar views:

[T]here is no room for the doctrine of estoppel operating to preclude the Commissioner from pursuing his statutory duty to assess tax in accordance with law. The Income Tax Assessment Act imposes obligations on the

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The availability of damages utilising s 22 of the

3. NON-JUDICIAL AVENUES FOR BUSINESSES SEEKING MONETARY COMPENSATION FOR TAX OFFICIAL WRONGS

The nonjudicial alternatives for recovering compensation from the Commissioner of Taxation include damages payouts resulting from breaches of the Taxpayers' Charter, an investigation by the Commonwealth Ombudsman or from complaint to ATO Internal Complaints and the various options accessible via that avenue including ex gratia relief under the CDDA Scheme administered by the Department of Finance. This section discusses each of these options.

3.1 Recovering Compensation for Breach of the Taxpayers' Charter

The Taxpayers' Charter (the 'Charter') consists of a series of booklets released by the Commissioner of Taxation in 1997.⁴¹ The Charter lists taxpayer rights and obligations and Australian Tax Office standards of service, although none of these booklets are specifically aimed at business. The Charter has no legislative force⁴² and does not actually create any additional legal rights for taxpayers.⁴³ However, the Charter

⁴¹There was a substantial review of the Charter in 2003. A revised version was introduced in November of that year. The Charter publications are Australian Taxation Office, Taxpayers' Charter: What You

publications envisage the possibility of awards of compensation for breaches of some Charter commitments. For example, the Commissioner in his publication Taxpayers' Charter – What You Need to Know states that '[i]n some circumstances you may be entitled to be paid compensation⁴⁴ however the entitlement to compensation for a breach of any of the commitments set out in

Nevertheless, any finding by the Commonwealth Ombudsman that the Commissioner should pay compensation to an aggrieved business taxpayer is not enforceable.⁵⁰ The sanction for ensuring the adoption of Commonwealth Ombudsman recommendations is the threat of adverse publicity. This is usually a sufficient incentive,⁵¹ however Bentley has questioned the perceived effectiveness of this sanction in the taxation context:

There is a perception among taxpayers that bad publicity would seldom in fact prevent any revenue organisation from exercising its powers to the fullest extent possible when it felt it was in the right, whatever the rights of the taxpayers involved.⁵²

If this perception accords with reality, the ramifications for business are significant. This is because, while Ombudsman investigation may generate a positive result for a business taxpayer, such a result cannot be

Even if a business taxpayer compensation claim does not raise important or complex legal issues and is not for a large quantum, business taxation arrangements more frequently raise complex factual questions than individual taxpayer claims. Courts are arguably also the most appropriate forum for resolving these questions.⁷⁴ The reasons include the fact that evidence is typically recorded in written form enabling close analysis and scrutiny and witnesses can be cross-examined on the factual complexities.⁷⁵ Most pertinently, however, courts are well versed in resolving complex factual questions of causation, fault and assessment of damages.⁷⁶

Such complex factual questions are especially difficult to answer where a taxpayer's claim is for pure economic loss because economic loss claims are 'frequently the result of complex human relationships where the effects of any action can be particularly unpredictable.'⁷⁷ Further, economic loss claims raise particularly acute public policy concerns about 'floodn

Commissioner are owed exclusively to the Crown. This view may be correct but there is presently no express legislative backing for it.⁸⁰

Further, no judge has explained the reasons for deviation in tax cases from application of the usual private law principles for determining when public authorities owe duties to citizens.⁸¹ At a minimum, therefore, there is also a role for legislative clarification to either confirm or reject this judicial approach.

Any such legislative clarification could serve to confirm the boundaries of acceptable tax administration behaviour toward business taxpayers. Any resultant recognition that the Commissioner owes some private law duties to taxpayers would restore the operation of compensation as a signalling mechanism for those boundaries of acceptable tax administration behaviour. Such a legislative move would consequently serve as a valuable aid in maintaining the legitimacy and acceptability of the tax collection function of the Commissioner in the eyes of the business community.⁸²

Further, such legislative action could correct any current ‘feelings of frustration and alienation which breed adversity between individuals and institutions’ stemming from the current denial of effective private law avenues of compensatory relief.⁸³ If this is true, statutory clarification and confirmation of the availability of private law compensatory relief may also help to avoid ‘overtly adversarial relationships’ between business taxpayers and the Commissioner.⁸⁴

For example, the Commissioner might presently be well advised to adopt an aggressive and adversarial approach to judicial settlements, safe in the knowledge that recourse to the courts for aggrieved business taxpayers presently holds little prospect of success. Statutory clarification and confirmation of the availability of private law compensatory relief for business taxpayers could remove the attraction of such an aggressive and adversarial stance.⁸⁵

⁸⁰See the discussion in section 2 of this article and above at n 40

⁸¹For example, in the case of the tort of negligence, the scope of any duty of care of public bodies in Australia has historically been determined through application of a guiding principle or approach such as the ‘policy/operational dichotomy’ (for example, see the judgment of Mason J in *Sutherland Shire Council v Heyman* (1985) 157 CLR 424), various proximity-based approaches (for example, see the approach of Deane J in *Jaensch v Coffey* (1983) 155 CLR 549) and, more recently, through the consideration of various public policy issues as part of an explicit preference for an ‘incremental approach’ to determining novel or difficult tortious actions (the rationale for which was described by Brennan J in *Sutherland Shire Council v Heyman*). Each of these approaches require consideration and

To the extent that such legislative action might encourage the use of formal avenues for business taxpayer recovery of compensation from the Commissioner it would also enhance business trust and confidence in our system of tax administration by making it easier to assess the Commissioner's performance in instances with business taxpayers.⁸⁶ Given that currently most compensation claims are resolved via confidential settlements or other unreported means, it is presently difficult to independently assess ATO performance by measuring the incidence or severity of causing mistakes or wrongs by tax officials.

This lack of transparency does little to foster taxpayer trust. In fact, it may serve to erode trust by raising suspicions that via confidential settlements and other unreported resolutions of claims the Commissioner is presently 'purchasing illegality'⁸⁷ or that the Commissioner may be using informal resolutions of claims as a 'tool for diminishing the judicial development of legal rights.'⁸⁸

5.2 Legislating for General Clarity and Certainty of Business Taxpayer Rights

Beyond the clarification of business taxpayer private law rights to compensation via court action, there is a role for legislation to play in resolving a number of the general uncertainties stemming from the current heavy dependence on discr

any possible allegations of bias which could be directed at the present system, with its heavy dependence on discretionary self-enforced mechanisms such as the Taxpayers' Charter and appeal to ATO Internal Complaints. The ATO are keen to dispel such allegations.⁹² However, the potential for a perception of impartiality to be associated with any self-administered or government-administered system for monetary compensation clearly remains.⁹³ This is enough to erode taxpayer trust and confidence.

In general terms the elimination of the uncertainty associated with a system of business taxpayer rights to compensation which turns almost exclusively on uncertain discretionary avenues of relief has much to recommend it. Uncertainty has been linked to taxpayer non-compliance⁹⁴ and its elimination features prominently as a core underlying value of any model of a desirable tax system.⁹⁵

The uncertainties inherent in the present system of discretionary self-administered avenues of compensatory relief which could be addressed by a formal legislative statement of business taxpayer rights to compensation are readily apparent. For example, with mechanisms such as the ATO Internal Complaints and the Taxpayers' Charter, the ATO decides the scope of application of the remedy and the levels of compensation available. They can change the criteria or withdraw the avenue of relief

Non-judicial discretionary avenues of relief are unsuitable for resolving many business taxpayer claims. In particular, the existing non-judicial options for recovery are inappropriate for resolving business claims which are factually complex, are for large quantum and/or raise serious legal questions. Thus, in such cases, business taxpayers are left with no suitable remedy.

In light of these findings, this article advocates legislative intervention to clarify the legal rights of business taxpayers to compensation for wrongs of tax officers. Two measures are specifically called for: clarification of the Commissioner's private law duties to taxpayers and a legislatively binding general pronouncement of business taxpayer rights to compensation.

It is conceded that this legislative intervention is likely to bring about an incidental extension of business taxpayer rights to compensation for tax official wrongs. However, this paper has not sought to advocate for any per se extension of business taxpayer rights to compensation. Instead, this paper has called for legislation principally aimed at providing a clear backdrop of legal rules for determining business taxpayer compensation claims. This paper has demonstrated that there are likely to be significant benefits in terms of fostering business taxpayer trust and confidence in our system of tax administration which, of themselves, justify this type of legislative clarification.

In short, this article has stressed the importance of business taxpayer compensation claims for loss caused by tax official wrongs being dealt with in a clear and legally certain environment. This is a minimum requirement for fostering an environment of business confidence and trust in our tax administration system. It is also a minimum requirement for the proper administration of justice.

The reform recommendations in this paper undoubtedly burden legislators with the responsibility for dealing with difficult questions of public policy, taxpayer rights and tax administration standards. It is clear, though, that legislators ultimately need to take the lead in dealing with these issues rather than leaving judges, the Commonwealth Ombudsman and the Commissioner himself to operate largely in a legislative vacuum in determining business taxpayer compensation claims.

This legislative vacuum has allowed the inadequacies in the current system for compensating business taxpayers for losses caused by the wrongs of tax officials exposed by this paper to flourish. This article provides a primer for the filling of that vacuum. From this position we are less likely to see any further unconscious 'erosion of civil rights in the name of exaction of taxes'¹⁰⁰