



FINANCIAL PLANNING
ASSOCIATION *of* AUSTRALIA

24 October 2016

ATO Penalty Project

Australian Taxation Office

PO Box 9977

CHERMSIDE QLD 4032

Email: FeedbackATOPenalties@ato.gov.au

Re. Proposed changes to penalties for small business and individuals

Dear Sir/Madam,

The Financial Planning Association of Australia (FPA) welcomes the opportunity to provide feedback on the ATO's proposed changes to penalties for small business and individuals. We welcome measures to ease the compliance burden for taxpayers. However, we also wish to ensure the proposed changes are sustainable. With this in mind, we have provided comments and recommendations for your consideration.

If you have any queries or comments, please do not hesitate to contact me at policy@fpa.com.au or on 02 9220 4500.

Yours sincerely

Dimitri Diamantes

Policy Manager

Financial Planning Association of Australia¹

¹ The Financial Planning Association (FPA) has more than 11,000 members and affiliates of whom 9,000 are practising financial planners and 5,500 CFP professionals. The FPA has taken a leadership role in the financial planning profession in Australia and globally:

- Our first "policy pillar" is to act in the public interest at all times.
 - In 2009 we announced a remuneration policy banning all commissions and conflicted remuneration on investments and superannuation for our members – years ahead of FOFA.
 - We have an independent conduct review panel, Chaired by Mark Vincent, dealing with investigations and complaints against our members for breaches of our professional rules.
 - The first financial planning professional body in the world to have a full suite of professional regulations incorporating a set of ethical principles, practice standards and professional conduct rules that explain and underpin professional financial planning practices. This is being exported to 24 member countries and the 150,000 CFP practitioners that make up the FPSB globally.
 - We have built a curriculum with 17 Australian Universities for degrees in financial planning. As at the 1st July 2013 all new members of the FPA will be required to hold, as a minimum, an approved undergraduate degree.
 - CFP certification is the pre-eminent certification in financial planning globally. The educational requirements and standards to attain CFP standing are equal to other professional bodies, eg CPA Australia.
 - We are recognised as a professional body by the Tax Practitioners Board
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PROPOSED CHANGES TO PENALTIES FOR SMALL BUSINESS AND INDIVIDUALS

FPA submission to:
ATO

24 October 2016

INTRODUCTION

The FPA welcomes efforts to give taxpayers a chance that's exercised as a matter of course, for failure to lodge on time and failure to take reasonable care. This measure would ease the compliance burden for taxpayers (including clients of financial planners) by the ATO providing education in place of penalties for certain breaches. However, we want to make sure that taxpayers are treated consistently and that the proposed policy is sustainable. With this in mind, we have raised some issues and possible solutions to challenges raised by the proposed policy.

Consultation Questions

1. Do you foresee any issues or unintended consequences with the approaches suggested above? If so, what are they and how important are they?

Where the risk to the government from a taxpayer failing to lodge on time or failing to take reasonable care is insignificant, there might be an argument that the extra costs of calculating a penalty are not worthwhile. However, this approach is less likely to benefit the government where a taxpayer is, as a matter of course, not penalised for multiple failures detected around the same time. Not only are there likely to be efficiency gains in calculating, at the same time, multiple penalties for the taxpayer, but the taxpayer is more likely to have a poor attitude to managing their tax affairs and so be a higher risk to the government.

Depending on the timing of detection, the benefit of the chance to the taxpayer might, therefore, be vastly greater if they have multiple failures. Unless appropriately bounded, the policy might therefore be unfit for purpose as taxpayers might be encouraged to maximise their benefit from the policy. For example, in the current financial year a taxpayer lodges their tax returns for the previous five financial years. There are multiple issues of failure to take reasonable care in each return. The same issues apply across multiple financial years. The ATO lodges notices of assessment shortly after the taxpayer lodges their returns, and later in the current financial year commences an examination of the taxpayer in respect of all returns lodged that financial year. The one chance policy has never been applied to the taxpayer.

It is not clear, as a matter of principle, whether the chance should apply for the whole period being examined (including any financial years brought in after the review commences) or just for a single instance of lateness and a single instance of failure to take reasonable care. If a reset period applies, the same taxpayer may again lodge multiple returns at once after the reset period. Again, it is not clear in principle how the one chance should apply. Both issues would need to be resolved empirically.

It may turn out that for all but one-off instances of failure to lodge on time, or failure to take reasonable care, that happen where the taxpayer has an otherwise unblemished recent tax record, a chance shouldn't be given as a matter of course. This is because beyond this limit, the benefits of calculating penalties are likely to outweigh the costs. However, it may again become cost effective for government to give the same taxpayer another chance if there is a subsequent review. This would support a reset period.

An alternative basis for a one chance policy and a reset period is that the cost to an individual or small business for complying with their tax affairs – after adjusting for differences in complexity – is likely to be higher, relative to income, for individuals and small businesses than other taxpayers. This difference would be problematic if we accept that the current level of people's proper tax rates relative to each other is right. An appropriately bounded one chance policy and reset period for individuals and small business taxpayers would mitigate this possible distortion of tax policy. The policy would still need to be appropriately bounded so as to approximately restore taxpayers to the ideal position relative to each other. The remainder of this paper follows from this alternative basis.

Recommendation

We recommend that, for small businesses and individuals, the policy might prescribe that, for the period under review, the chance applies only for:

- one return or activity statement that failed to be lodged on time that has the earliest lodgment date (or, for a return or activity statement that is not yet lodged, examination notification date); and, in addition
- one instance of failure to take reasonable care for the earliest financial year for which a failure to take reasonable care is identified by the ATO.

In other words, there should be one chance for failure to lodge on time and one chance for failure to take reasonable care, which could both, potentially, be applied with respect to the same return or activity statement.

Further, consideration should be given to prescribing that the one chance policy applies only once it is clear from the taxpayer's recent tax history that the taxpayer does not represent a significant risk to government revenue.

2. If a client uses their one chance, do you think the one chance should reset after a period of time? If so, how much time should pass before the one chance resets for income tax returns and activity statements (i.e., is available to a client again after they have already used their one chance?) If not, why not?

A reset period may be especially appropriate for small business and individuals because the one chance policy offsets the relatively higher compliance costs to these taxpayers.

Recommendation

We recommend that the reset period from an examination in which the ATO applies the chance, should be four years after the notice of assessment is issued for the return or activity statement in respect of which the chance is applied. Based on the time limits for amendment of tax notices, four years is long enough to ensure that the chance is applied by the time it is reset.

There should be a separate chance for failure to lodge and failure to take reasonable care. Each might have different start dates for the purpose of the reset period.

3. Are there any groups of individuals or small businesses you think should be denied the one chance approach? If so, what groups?

No group should be denied the one chance approach without good reason.

Recommendation

No sub-group should be denied the one chance approach unless it is clear that the cost of managing their tax affairs, adjusted for complexity and relative to income, is too low to warrant government support.

4. To help your future tax compliance as an individual or business, what specific information could the ATO provide on what the error was and show you how to fix it and how could we provide it?

Best practice would identify the error, show why it's an error and demonstrate the correct application of the rules.

Recommendation

We recommend that the ATO provide written guidance to the taxpayer and, where there is one, the tax agent. The guidance should identify the specific error, the relevant rules and the correct application of the rules.

5. Where a client has lodged via a tax or BAS agent or intermediary, to whom should the ATO provide information on what the error was and show how to fix it, and why? Tax or BAS agent/Intermediary; client; or both?

The challenge is to ensure that the taxpayer receives the information.

Recommendation

To ensure the taxpayer receives the information, we believe it would be prudent to send the information to them directly. In addition, where an intermediary, such as an agent, is involved, the information should be provided to the intermediary as well (subject to the intermediary being authorised to receive such information) so that the intermediary can assist the taxpayer in understanding the information and applying it in the future.

6. Would it change your perception of 'fairness of the system' if individuals and small businesses were given one chance to fix errors or improve on time lodgment with no penalty applied? If so, how?

As discussed, differences in the cost of managing tax affairs can move the allocation of the tax burden among taxpayers, away from the ideal. An appropriately bounded one chance policy would seek to offset this distortion, by returning the allocation of the tax burden to that which has been judged (through the political settlement) to be fair.

7. How do you think this will impact tax or BAS agents and intermediaries?

The measure may help agents and intermediaries maintain their relationships with clients. Even where the client hasn't been full and frank with the intermediary, a client that is charged a penalty may resent the intermediary. This has associated costs without necessarily providing real gains. By not determining a penalty, there is a better chance that these unnecessary costs will be avoided.

8. Do you have any other comments or suggestions?

We have no other comments or suggestions.