

INDEPENDENT TAX DISPUTE RESOLUTION AND SOCIAL JUSTICE IN AUSTRALIA

BINH TRAN-NAM* AND MICHAEL WALPOLE**

I INTRODUCTION

As a multidimensional concept, social justice clearly means different things to different people depending on their biases, perspectives or research interests. In a recent publication, the National Pro Bono Resource Centre provides a useful summary discussion on social justice, including historical development of the concept, themes of social justice formulations, and the relationship between social justice and concepts such as human rights and social inclusion.¹ In particular, that paper identifies a number of common themes that arise when examining different views on social justice. In terms of joint responsibility, these include the fair redistribution of resources, equal access to opportunities and rights, a fair system of law and due process, the ability to take up opportunities and exercise rights, and the protection of vulnerable and disadvantaged people.²

In view of the range of alternative approaches to social justice, it is necessary to commence with a definition of the concept in order to explain our perspective as well as the nature and focus of our article. To us, social justice means that every individual in a society has an intrinsic right to enjoy a minimum level of welfare and equal access to government services, including the legal system, regardless of his or her ability to contribute to the creation of wealth. This definition links social justice to other fundamental attributes of a civic society, such as human rights. Note that we perceive welfare in the spirit of Sen's capabilities approach,³ reaching beyond the more traditional and limited concept of material welfare. It is important to note also that our definition does not extend to those individuals who are capable but unwilling to contribute to the creation of wealth. Further, while our definition embraces some of the themes mentioned above, it is nevertheless restricted to the economic dimension of social justice.

* Associate Professor, School of Taxation and Business Law, Australian School of Business, University of New South Wales.

** Professor and Associate Head of School (Research), Australian School of Taxation and Business Law, Australian School of Business, University of New South Wales.

1 'What Is Social Justice?' (Occasional Paper No 1, National Pro Bono Resource Centre, October 2011).

2 Ibid 4.

3 See, eg, Amartya Sen, *Development as Freedom* (Oxford University Press, 1999).

Given that the specification of the social justice norm is highly contentious,⁴ it seems worthwhile to provide a brief discussion on the rationale for our adoption of the particular conception of social justice outlined above. Our emphasis on a minimum acceptable level of welfare and equal access to government services reflects an approach to social justice aimed at ensuring that people are not excluded from essential life opportunities, such as education, housing, health care and employment. A quick examination of Australian media reportage reveals that access to essential services in Australia has become an increasingly critical issue, despite the country's continuing growth and prosperity.

Even though our definition of social justice has been suitably restricted, it is nevertheless quite broad. As tax academics, we would naturally like to focus on our own area of expertise. Correspondingly, this article is primarily concerned with the tax dimension of social justice – which may be termed 'tax justice' or 'tax fairness' – where the term tax is broadly defined to include both taxes and transfers (and where transfers can be viewed as negative taxes).⁵ In fact, our choice of topic does not merely reflect our specialisation. The significance of tax justice is abundantly apparent in view of the fact that taxation is one of the more important (and most common) relationships between a citizen and the government.

Tax justice is itself a multidimensional concept. It can be interpreted differently in different contexts. In this article we make a distinction between two main elements of tax justice. The first aspect, frequently discussed in the public finance literature, is concerned with tax policy equity. Tax policy equity is concerned with the distribution of tax burdens among individuals in a society. The second aspect, mainly discussed in the tax administrative and legal literature, deals with tax procedural equity. This concerns the fairness of the procedures involved in tax audits and disputes, and the perceived treatment the taxpayer receives from the tax authority.⁶

Since tax policy equity has been comprehensively discussed in the public finance literature,⁷ only a very brief review is attempted here. Tax policy equity is based on the 'capacity to pay' principle, and often expressed in terms of

4 As evident by the critiques of John Rawls, *A Theory of Justice* (Harvard University Press, 1971). Some of the best-known criticisms of Rawls include Brian Barry, 'Liberalism and Want-Satisfaction: A Critique of John Rawls' (1973) 1 *Political Theory* 134; John C Harsanyi, 'Can the Maximin Principle Serve as a Basis for Morality? A Critique of John Rawls's Theory' (1975) 69 *American Political Science Review* 594; G A Cohen, *Rescuing Justice and Equality* (Harvard University Press, 2008); Amartya Sen, *The Idea of Justice* (Harvard University Press, 2009).

5 Although the article focuses on tax disputes, much of its analysis and arguments can also be extended to transfer disputes with minor modifications.

6 Suitably adapted from Kristina Murphy, 'Regulating More Effectively: The Relationship between Procedural Justice, Legitimacy, and Tax Non-Compliance' (2005) 32 *Journal of Law and Society* 562, 566.

7 See, eg, Richard A Musgrave and Peggy B Musgrave, *Public Finance in Theory and Practice* (McGraw-Hill, 5th ed, 1989) 218–32; Joseph E Stiglitz, *Economics of the Public Sector* (W W Norton, 3rd ed, 2000) 468–75.

horizontal and vertical equity.⁸ Needless to say, while horizontal and vertical equity are simple and intuitively appealing, they are very difficult to implement in practice. A further practical challenge to tax policy equity is the variation in compliance behaviour among individual taxpayers and in their opportunities to avoid/evade taxes. For example, tax evasion tends to happen relatively more often in business activities which are settled in cash without any reporting.⁹ This gives rise to unequal treatment between employees on payroll and certain types of self-employed persons.¹⁰

While issues related to tax policy equity are highly relevant to social justice, it is the second aspect of tax justice, namely tax procedural justice, on which we will focus in this article. This is so for a number of reasons. First, tax procedural justice encompasses matters such as the ways in which tax disputes are resolved, and how an individual taxpayer who disagrees with a decision of the Australian Taxation Office ('ATO') is treated by the ATO and the legal system. This immediately raises the issue of access by individual taxpayers to an independent tax dispute resolution procedure provided by the government. The issue of accessibility to such a process is consistent with the definition of social justice articulated at the beginning of this article.

Second, while public policy considerations tend to dominate tax policy equity debates, tax procedural justice brings to the fore the role of the legal system in devising policies that promote social justice. Third, tax procedural justice is not a frequently discussed topic relative to tax policy justice. While tax debates are mostly concerned with the actual (potential) efficiency, policy equity and simplification impacts of existing (proposed) tax reform measures, relatively little public attention has been paid to tax procedural justice. We think it is, therefore, timely to contribute to this important but under-explored topic.

The principal aim of this article is thus to examine the current tax dispute resolution in Australia from a social justice perspective. As mentioned previously, procedural justice in the context of taxation can be considered as comprising two separate elements: how the taxpayer is treated by the ATO, and access to an external process for resolving tax disputes. The focus of the paper is on the second element of tax procedural justice, that is, effective access to a fair, impartial and independent process of dispute resolution. The correctness, or otherwise, of the outcome of the process is obviously important but beyond the scope of this article. Further, in principle, there are several types of tax disputes and some of them do not involve the ATO as a party. These may arise between two or more parties in a legal agreement or commercial dealing. For example,

8 Musgrave and Musgrave, above n 7, 223; Stiglitz, above n 7, 468–9.

9 See, eg, Cynthia Coleman and Chris Evans, 'Tax Compliance Issues for Small Business in Australia' in Neil Warren (ed), *Taxing Small Business: Developing Good Tax Policies* (Australian Tax Research Foundation, 2003) 147; Martti Vihanto, 'Tax Evasion and the Psychology of the Social Contract' (2003) 32 *Journal of Socio-Economics* 111, 113.

10 See, eg, Ken Devos, 'Tax Evasion Behaviour and Demographic Factors: An Exploratory Study in Australia' (2008) 18 *Revenue Law Journal* 1, 12; Susan Cleary Morse, Stewart Karlinsky and Joseph Bankman, 'Cash Businesses and Tax Evasion' (2009) 20 *Stanford Law and Policy Review* 37.

one of the parties may disagree with the meaning of a contractual agreement, or the operation of a statute, and whether or to what extent a tax is payable by one of the parties. These types of disputes are beyond the scope of this article, since we have confined ourselves to tax disputes to which the ATO is a party.

The organisation of the remainder of this article is as follows: in Part II, we consider how tax disputes fundamentally differ from other types of disputes. This is necessary to make the case for a special study of tax disputes, rather than a study of disputes in general. In Part III we discuss the meaning of tax disputes, how they arise and the mechanism for resolving them in Australia. This section demonstrates that Australians enjoy an elaborate and established system of independent tax dispute resolution. In Part IV we study the practical accessibility to independent tax dispute resolution in Australia. It is argued that the Australian system of independent tax dispute resolution is ineffective, in the sense that the full costs of tax dispute resolution to the taxpayer are so high that only a very small fraction of taxpayers in dispute with the ATO make use of the system. The consequences of such inaccessibility, especially the consequences for social justice, are examined in Part V. Some concluding remarks and policy recommendations are then given in the final section.

II WHY TAX DISPUTES?

Disputes are a common feature of any human society, regardless of time, space, social traditions or level of development. In fact, disputes are by no means confined to humans alone. In a modern society, they can arise in many areas of life, and involve all stakeholders of the society, including individuals, businesses, organisations and government departments. Why do tax disputes require special attention? Are they fundamentally different from other types of disputes? Tax disputes are in many ways an example of administrative disputes. Parties involved in those disputes are required to make genuine efforts to settle, via alternative dispute resolution ('ADR'), before these disputes can be settled by judicial determination. Nevertheless, tax disputes also possess a number of special attributes that will be elaborated upon below.

First, tax laws, particularly income tax law, tend to be more complex than civil or commercial laws.¹¹ When the federal income tax was introduced as a wartime measure in 1915, it was a minor and relatively simple tax. Over the years, especially from the mid-1980s,¹² income tax has grown to become the

11 For a detailed discussion on the complexity of the current Australian tax system in terms of conventional measures of tax complexity such as number of taxes, length and readability of tax law, reliance on tax agents and tax compliance costs, the interested reader is referred to Chris Evans and Binh Tran-Nam, 'Managing Tax System Complexity: Building Bridges through Pre-Filled Tax Returns' (2010) 25 *Australian Tax Forum* 245.

12 In the mid-1980s, the Labor Government substantially widened the income tax base through the introduction of the Capital Gains Tax and the Fringe Benefits Tax.

most significant source of revenue for the Australian government.¹³ During the same periods, income tax law has become disproportionately more complex. For example, the length of the *Income Tax Assessment Act 1936* (Cth) ('*ITAA 1936*') has increased from 126 pages at its inception to over 5743 in 2008. The combined length of the *ITAA 1936* and the *Income Tax Assessment Act 1997* (Cth) ('*ITAA 1997*') now stands at about 7000 pages, after the recent removal of a significant number of pages (close to 30 per cent) of inoperative provisions in the two Acts.

Not surprisingly, tax academics, practitioners and judges have been united in their views regarding the complexity of Australian tax laws. Over 20 years ago, Jeffrey Waincymer, a leading tax law professor, made the following remarks about Australian income tax law:

The law is voluminous ... [and] has inherent ambiguities. Many of the core concepts are not defined and have been left to the courts to develop. Some are virtually indeterminate. Many have no justification in policy terms. There are numerous disputes.¹⁴

The Commonwealth Attorney-General's Department agreed, claiming that 'existing tax laws ... are complex and in a form not easily understood by most people'.¹⁵ The late Hill J also concurred, stating that the legislation was 'drafted with such obscurity that even those used to interpreting the utterances of the Delphic oracle might falter in seeking to elicit a sensible meaning from its terms'.¹⁶ Sadly, the Tax Law Improvement Program ('TLIP') undertaken by the Australian Government in the 1990s has had little impact in terms of legal simplification.¹⁷

Second, there is a reversal of roles when tax disputes are considered by the Tribunal or the courts. While there are no formal plaintiffs and defendants in tax disputes, it is the taxpayer (who applies to the Tribunal or the courts) who can be regarded as playing the role of the plaintiff. This is the case despite that fact it is the Commissioner of Taxation who obliges the taxpayer to pay the amount of tax in dispute. This is clearly a role reversal in comparison with civil dispute cases. A rationale that has often been advanced to justify this reversal is that there is an asymmetry of information between the two parties. That is, the taxpayer is supposed to possess all the facts and information about his or her personal tax affairs, while the Tax Commissioner does not.

13 In 2009–10, income tax revenue accounted for 70 per cent of the Australian Federal Government's tax revenue; see Australian Bureau of Statistics, *Year Book Australia, 2012* (ABS Catalogue No 1301.0, 24 May 2012) 756, table 28.9.

14 Jeffrey Waincymer, *Australian Income Tax: Principles and Policy* (Butterworths, 1991) 66.

15 Attorney-General's Department (Cth), *The Justice Statement* (1995) 122.

16 *Federal Commissioner of Taxation v Cooling* (1990) 22 FCR 42, 61 (Hill J). A further example of the complexity of the *ITAA 1936*, as encountered by the Full High Court, is found in its final orders in *Hepples v Federal Commissioner of Taxation* (1992) 173 CLR 492 ('*Hepples*') where similar sentiments to Justice Hill's were expressed.

17 Binh Tran-Nam, 'Tax Reform and Tax Simplicity: A New and "Simpler" Tax System?' (2000) 23 *UNSW Law Journal* 241.

It is interesting to note that when an objection is being reviewed before the Tribunal or appealed to a court, the burden of proof rests on the taxpayer making the objection.¹⁸ It is up to the taxpayer to demonstrate to the Tribunal or the court that either the ATO's assessment was excessive, or that the ATO's decision should not have been made, or that it should have been made differently. The fact that the burden of proof lies with the taxpayer is consistent with the role reversal discussed above, but not with the principle of presumption of innocence (according to which it is up to the Commissioner to prove that his or her assessment is correct).

Third, unlike most civil or commercial disputes, tax disputes typically involve a perceived asymmetry between the two parties concerned. Most taxpayers who are in dispute with the ATO, whether actually or potentially, are individuals. Of course, taxpayers who are in dispute with the ATO also include corporate taxpayers, and some of them can be very large and powerful. However, bearing in mind the aims of the present article, we focus on individual taxpayers, including sole traders and partners, to whom the issue of social justice is possibly relevant.

Individual taxpayers tend to face severe time constraints and, in the main, financial constraints also. Of course, there are individual taxpayers who have high profiles (such as actor Paul Hogan¹⁹) or great wealth (such as Glenn Wheatley²⁰) or expertise in tax matters, but they are exceptions rather than the norm. On the other hand, the ATO is a powerful and influential government organ, with many employees and considerable financial resources. They can draw, if they so wish, technical and legal advice from not only a critical mass of their own employees, but also a vast array of external tax and legal experts. The apparent inequality of positions between the ATO and taxpayers was officially recognised in a recommendation by the Joint Committee of Public Accounts, leading to the creation of the title of Tax Ombudsman in 1995.²¹

The Tax Commissioner's bargaining position may in fact be more limited than depicted above. As mentioned previously, there is an asymmetry of information in favour of the taxpayer. It would be quite costly for the ATO to obtain all of the facts concerning a taxpayer's personal tax affairs without his or her cooperation. Further, while the Tax Commissioner clearly has more resources available to him or her in the aggregate than most individual taxpayers, these resources must be allocated amongst the ATO's many tasks. Thus, the Commissioner still faces resource scarcity, and must make choices much as individual taxpayers do. In fact, the settlement of tax disputes by 'good

18 *Taxation Administration Act 1953* (Cth) ss 14ZZK(b)(i), 14ZZO(b)(i) ('*Taxation Administration Act*').

19 Bonnie Malkin, 'Crocodile Dundee Paul Hogan's Off-Shore Tax Accounts to be Published', *The Telegraph* (online), 16 June 2010 <<http://www.telegraph.co.uk/news/worldnews/australiaandthepacific/australia/7832537/Crocodile-Dundee-Paul-Hogans-off-shore-tax-accounts-to-be-published.html>>.

20 Melissa Jenkins and Mariza O'Keefe, 'Wheatley Sent to Jail Over Tax Fraud', *Sydney Morning Herald* (Sydney), 20 July 2007.

21 Commonwealth Ombudsman, *Annual Report 2010–2011* (2011) 134 ('*Commonwealth Ombudsman Annual Report 2010–11*').

administration rule' reflects, in part, the recognition of the Commissioner's limited resource availability.²² Further, the Commissioner is also bound by constraints that may not be relevant to the taxpayer, such as the model litigant rules, and the inability to publicise via mass media.

Fourth, tax disputes differ fundamentally from other civil and commercial disputes and criminal trials in terms of impact. The court decisions arising from tax dispute cases constitute a source of case law, which can affect the lives of many people to whom the law applies. Although this may be true of other disputes, tax disputes and the legal ramifications of court decisions in them have a high level of generality and applicability to other taxpayers. This raises the stakes, as a loss in one tax case may amount to a loss in hundreds of other cases involving taxpayers in similar circumstances, such that the resolution of a tax dispute by a court automatically has a class-action effect. To put it more bluntly, while a taxpayer only sees a \$500 deduction, the Commissioner (really the broader Australian community) might see a \$50 million threat to tax revenue.

Fifth, unlike most civil and commercial disputes, the two parties to a tax dispute are also unevenly positioned with respect to the ability of each to influence the law after the court's judgment has been handed down. Taxpayers, whether individual or business, must take tax laws as given and rely, ultimately, on the courts' judgments to settle their disputes with the ATO.²³ They can only influence tax law indirectly, through collective actions such as lobbying, or by exercising their votes in an election. On the other hand, if the Tax Commissioner's decision is not upheld by the courts, the ATO (or Treasury) can directly approach the federal government to pass new legislation to prevent such losses in the future. Some illustrative examples are the changes to deductibility of expenses incurred by criminals pursuant to the decision in *Federal Commissioner of Taxation v La Rosa*,²⁴ and the change to deductibility of education expenses against Austudy allowances in response to the decision in *Federal Commissioner of Taxation v Anstis*.²⁵ In both cases, the law was changed after the Commissioner lost in court.²⁶ Note that this is not an uncommon feature of administrative disputes that involve a government agency or department as a party.

Finally, it is also worthwhile to briefly mention the ATO's test case litigation program.²⁷ There are important issues where it is in the public interest to have the tax law clarified through litigation. Since the ATO cannot commence such litigation, they are willing to provide financial assistance to taxpayers to do so in

22 Australian Taxation Office, *Code of Settlement Practice* (23 December 2011) <<http://www.ato.gov.au/corporate/content.aspx?doc=/content/8249.htm>> ('*ATO Code of Settlement Practice*').

23 It is worthwhile to note at this stage that a vast majority of tax disputes do not proceed to the courts.

24 (2002) 196 ALR 139.

25 (2010) 241 CLR 443.

26 Note that the fact that a tax law has been amended after the court decision does not affect the relative positions of the parties to the dispute with respect to that dispute.

27 Australian Taxation Office, *Test Case Litigation Program* (9 June 2009) <<http://www.ato.gov.au/taxprofessionals/content/57395.htm>>.

order to develop legal precedents to such issues. There are also some test cases initiated by the ATO through its public rulings program. In those cases, funding can be offered without the need for an application. In other cases, taxpayers need to make applications for funding, and selection is made by a test case litigation panel that includes members of the accounting and legal professions.²⁸

To summarise, tax disputes differ from other civil and commercial disputes in some fundamental ways. This justifies the need to consider the social justice dimension of tax disputes separately. Having argued that, it is now our intention to define tax disputes more formally, and to explain how they can be resolved in Australia at present.

III PROCESS OF TAX DISPUTE RESOLUTION IN AUSTRALIA

A Meaning and Types of Tax Disputes

Tax disputes between taxpayers and the central revenue collection agency are a common feature of modern tax systems around the world. Conventionally, they are said to occur when taxpayers disagree with the view provided by the tax administration in respect of their tax liabilities or entitlements and related issues. In this article, we adopt a more restrictive definition. Tax disputes are said to take place when the taxpayer takes a contrary view to that of the tax administration, and decides to take some action regarding this disagreement. This definition does not include those cases in which taxpayers disagree with tax administrators but do not take any action apart from complying with the decisions of tax administrators. Our choice of a more restrictive definition is dictated mainly by the fact those taxpayers who disagree but do nothing about it are unobservable to independent researchers.

Tax disputes may arise at any stage after the disagreement between the tax administration and taxpayers. In Australia, they are classified into four broad categories:

- (a) complaints;
- (b) objections to reviewable rulings;
- (c) disputes as to facts or the application of tax law by a taxpayer as matters are being assessed (by the ATO); and
- (d) objections to assessments (including self-assessment and Commissioner-made adjustments).²⁹

28 In 2010–11, there were 12 test-case decisions. Eight of these clarified the law, while the other four resulted in the government announcing some changes in the law; see Australian Taxation Office, *Your Case Matters 2012: Tax and Superannuation Litigation Trends* (2012) 12.

29 Michael D'Ascenzo, 'In Search of Solutions' (Speech delivered at the Administrative Appeals Tribunal and the ACT Bar Association Seminar – The Obligation to Assist: Model Litigants in Administrative Appeals Tribunal Proceedings, Canberra, 26 August 2009).

Categories (b) and (d) generally refer to statutory rights, while (a) and (c) relate to administrative due process.

B How Do Tax Disputes Arise?

Tax disputes under the current self-assessment system in Australia are only likely to occur in two main situations: where a taxpayer follows a ruling with which they disagree, and then objects to the assessment based on the ruling; and where an amended assessment has been made after an audit of a return.³⁰ Note that an amended assessment can be issued after a variety of circumstances, including an audit or data matching activity (section 170 of the *ITAA 1936* amended assessment) or default assessment (section 167 of the *ITAA 1936*), or an ‘assets betterment’ assessment. As in other jurisdictions with self-assessment, tax disputes between taxpayers and the ATO principally arise through an audit, as described below.³¹

Most Australian taxpayers have an obligation to provide the details of their taxable income on an annual basis. On that basis, the Tax Commissioner is required to raise an assessment under section 161 of the *ITAA 1936*, and to provide that assessment to the taxpayer. Where there is a tax debt, the taxpayer is obliged to pay that debt by the due date. Otherwise, where there is a tax refund due, that amount will be repaid by the ATO.³² Under self-assessment, the ATO would normally raise an assessment based on the information provided in the tax return. There may be a pre-assessment query issued by the ATO,³³ a rejection of a claimed deduction, or an inclusion of an amount of income (such as undisclosed interest or dividends).

A dispute between a taxpayer and the ATO would typically commence at the point at which the assessment is under review. There may be an audit of the taxpayer’s affairs, or a post-assessment review of these affairs. For example, there may be an audit of income or expenditure items in the taxpayer’s return. There may also be post-assessment reviews, such as for a rental property and associated claims in connection with that property. In the period following post-assessment, an informal dispute may be considered as occurring. If this dispute cannot be resolved, then an assessment will be issued by the ATO, with the result of amended taxable income. At this point the taxpayer may formally lodge an

30 Suzette Chapple, ‘Income Tax Dispute Resolution: Can We Learn from Other Jurisdictions?’ (1999) 2 *Journal of Australian Taxation* 312, 318.

31 In 2010–11, about 72 per cent of objections to income tax assessments arose directly from the ATO’s audit and review activities: Australian Taxation Office, above n 28, 4.

32 Delays in receiving tax refunds have been a major source of complaints by individual taxpayers. The number of complaints about tax refund delays have increased substantially in the past few years as a result of the ATO’s IT upgrade, known as the Change Program: see Ron Brent, Commonwealth Ombudsman, *Review into the ATO’s Change Program* (2010). Many individual taxpayers mentioned financial hardship in their complaints.

33 Pre-assessment checks may also cause delays in tax refunds, although in this case interest is paid by the ATO to taxpayers who are entitled to receive tax refunds. The ATO’s recent increase in pre-assessment checks have resulted in delays in issuing tax refunds, which have in turn caused financial hardship to some taxpayers.

‘objection’, in accordance with part IVC of the *Taxation Administration Act* and section 175A of the *ITAA 1936*. The tax dispute has formally commenced at this stage.

C How Can Tax Disputes be Resolved?

Tax disputes between taxpayers and the ATO can be resolved by various methods and mechanisms. Methods for resolving disputes include negotiation, mediation, arbitration and judicial adjudication, whereas dispute resolution mechanisms include the ATO’s internal review, the Administrative Appeals Tribunal (‘AAT’) and the courts. To avoid the expense of tax litigation before the courts, there has been an emphasis on ADR, which ‘is an umbrella term of process, other than judicial determination, in which an impartial person ... [assists] ... those in dispute to resolve the issues between them’.³⁴

ADR often takes the form of negotiation, mediation and arbitration, as elaborated below:

- Negotiation (no third party): ‘Negotiation takes place where the parties in a dispute, with or without partisans in support of the respective disputants, approach each other without the assistance of any third party and seek a mutually acceptable outcome through discussion’.³⁵ This is the principal method employed by the ATO for resolving tax disputes.
- Mediation (with mediator): ‘Mediation is a decision-making process in which the parties are assisted by a third party, the mediator; the mediator attempts to improve the process of decision-making and to assist the parties reach an outcome to which each of them can assent’.³⁶ Mediation has been a common process for resolving tax disputes at the AAT.³⁷
- Arbitration: Arbitration can be private (informal) or public (formal). In the tax context, arbitration is a public adversary process that provides an objective, independent and impartial determination of disputed facts or issues by legal experts appointed by the government. The AAT provides an example of formal arbitration, in the sense that it is not private and the outcome is binding on the parties.

The process of tax dispute resolution in Australia is comprehensive and essentially consists of three layers: ATO (internal, ADR), AAT (external, ADR, administrative) and the courts (external, judicial review). This is illustrated in Figure 1.

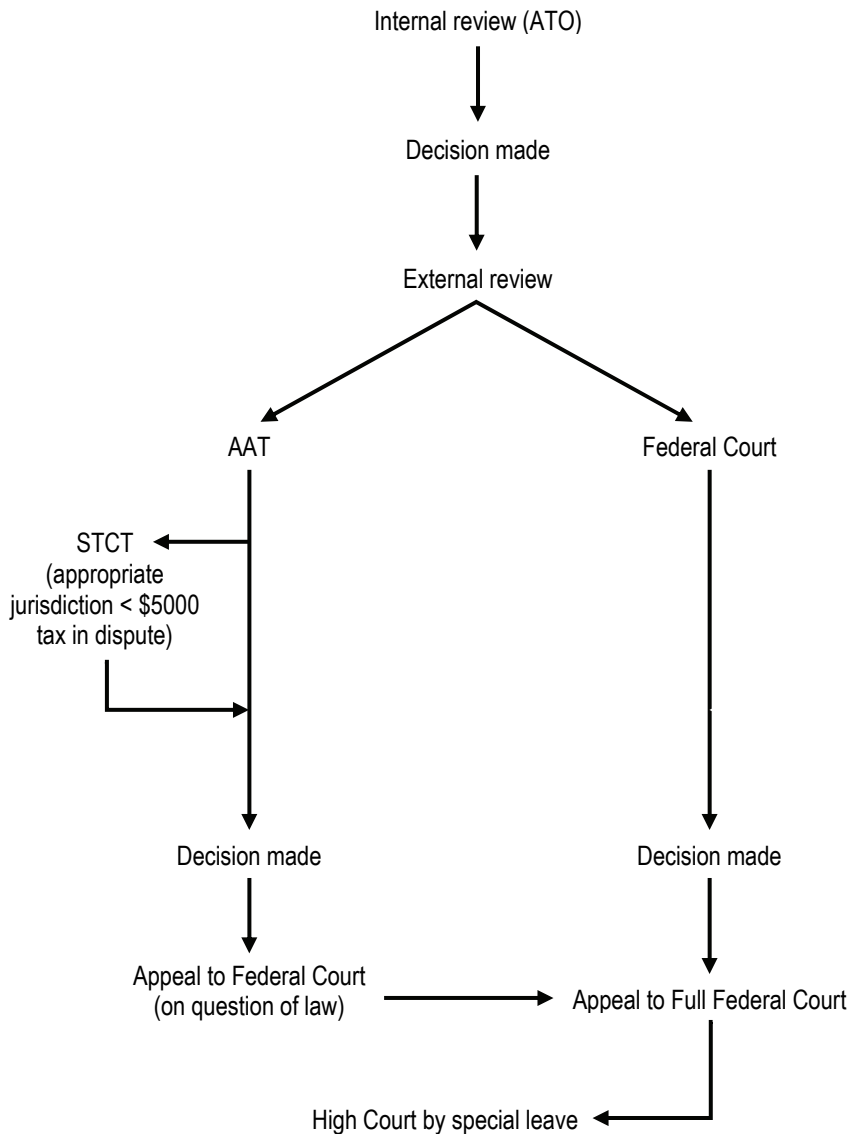
34 National Alternative Dispute Resolution Advisory Council, *Dispute Resolution Terms: The Use of Terms in (Alternative) Dispute Resolution* (2003).

35 Duncan Bentley, ‘Problem Resolution: Does the ATO Approach Really Work?’ (1996) 6 *Revenue Law Journal* 17, 19.

36 Laurence Boule, *Mediation: Principles, Process, Practice* (Butterworths, 1996) 3.

37 Mediation is provided by the AAT via conferences. According to recent statistics (from 2008–09 to 2010–11), about 80 per cent of tax applications to the AAT have been finalised without a hearing: see Administrative Appeals Tribunal, *Annual Report 2010–11* (2011) 132 (‘AAT Annual Report 2010–11’).

Figure 1: The Current Process of Tax Dispute Resolution in Australia



Note that, in addition to the above mechanisms, the Commonwealth Ombudsman, the Inspector General of Taxation and, to a much lesser extent, the Australian Human Rights Commissioner and the Australian Information Commissioner can examine how specific taxpayers have been treated by the ATO. In the context of resolving tax complaints and social justice, it is worthwhile to elaborate on the role of the Commonwealth Ombudsman. As

mentioned in Part II, following a recommendation by the Joint Committee of Public Accounts, in 1995 the Ombudsman was given the title of Taxation Ombudsman to give greater focus to the investigation of complaints about the ATO. In 2010–11, there were 2589 complaints about the ATO, representing about 13 per cent of all complaints received by the Ombudsman.³⁸ While the overall trend in complaint about the ATO has been increasing since 2007–08, the significant increase in 2010–11 (43 per cent more than 2009–10) was primarily attributable to delays in processing income tax returns that resulted from the ATO's Change Program, mentioned previously.³⁹ The main complaint themes include lodgement and processing (including refunds), taxpayer information, debt collection, audit, superannuation and 'other'. Note that the Taxation Ombudsman typically only investigates a fraction of complaints received (21 per cent in 2010–11, and 18 per cent in 2009–10).⁴⁰

D The ATO's Internal Review

Part IVC of the *Taxation Administration Act* provides a standardised review and appeal mechanism for the approach to be taken for tax dispute resolution. It is important to note that the appropriate link between the *ITAA 1936* and part IVC of the *Taxation Administration Act* is section 153 of the *ITAA 1936*. That section provides the legislative basis for a taxpayer wishing to object to an assessment (which includes an amended assessment) to do so in accordance with the provisions of the *Taxation Administration Act*. When a valid objection has been lodged, an internal review of the assessment will be conducted by ATO officers. Note that the internal review relates to matters raised in that objection, and not in respect of the entire assessment. Sixty days must pass before the taxpayer can demand a decision to the objection. If no objection decision is available after 60 days, section 14AYA(2) of the *Taxation Administration Act* permits the taxpayer to make a written request to the Commissioner for an objection decision within a further 60 days. When the objection has been disallowed or allowed only in part, or has been deemed to be disallowed (where no decision has been given after a further 60 days), further review opportunities for the taxpayer are triggered.

According to the Commonwealth Attorney-General's *Legal Services Directions 2005*, the ATO, as a 'model litigant', is required, where possible, to avoid, prevent and limit the scope of legal proceedings.⁴¹ This includes giving consideration in all cases to ADR before initiating legal proceedings, and participating in ADR where appropriate. The Commissioner of Taxation has instructed ATO staff responsible for resolving tax disputes to consider participating in some form of ADR throughout the course of the dispute.⁴²

38 *Commonwealth Ombudsman Annual Report 2010–11*, above n 21, 5–6.

39 *Ibid* 134–5.

40 *Ibid* 135.

41 *Legal Services Directions 2005* (Cth) para 4.2, app B.

42 *ATO Code of Settlement Practice*, above n 22, [37].

Further, both the AAT and Federal Court may direct the ATO to participate in certain ADR proceedings.⁴³ The most recent change in this respect is the introduction of the *Civil Dispute Resolution Act 2011* (Cth), which requires all parties appearing at the Federal Court to demonstrate to the satisfaction of the judge that they have made genuine efforts to resolve their dispute before coming to a formal hearing before the Court. The Federal Court rules have also been amended to give effect to this.

As suggested previously, tax audit is a vitally important tool in tax enforcement under self-assessment. Not surprisingly, tax disputes principally arise through an audit.⁴⁴ Because of the inherent uncertainty in the interpretation and application of tax laws, audits often conclude with a negotiated settlement.⁴⁵ For example, a tax auditor might arrive at a position regarding a taxpayer's tax liability, but then, after consultation with the taxpayer, accept that the audit position is not correct.⁴⁶ Thus, in practice, the vast majority of objections are finalised by negotiations during internal review by the ATO. As pointed out by Chapple, the ATO's internal review process is 'undermined by the absence of any obligation for the Commissioner to provide detailed reasons for an assessment or the objection decision together with the poor communication of such reasons'.⁴⁷

E The Administrative Appeals Tribunal

The taxpayer has a choice as to the appropriate external review body. The taxpayer may either refer the objection decision to the AAT, or appeal to the Federal Court. In principle, it is the taxpayer's choice, and the ATO has no hand to play in which review body is chosen. It is important to note that, as an administrative review body, the AAT is fundamentally and structurally different from the Federal Court, which is a judicial review body. These differences will be elaborated in this Section, and in Section F below.

The AAT was established by the *Administrative Appeals Tribunal Act 1975* (Cth) ('*AAT Act*'), and commenced to operate in 1976, replacing the Boards of Review, which were introduced in 1922.⁴⁸ The AAT, being an administrative body, is able to 'stand in the shoes' of the Commissioner of Taxation, and re-examines all powers and discretions available that are relevant to the objection decision. In its arbitration of tax disputes, the AAT may affirm, set aside, vary, remit or dismiss the objection decision, while the Federal Court can confirm or

43 *Administrative Appeals Tribunal Act 1975* (Cth) s 34A; *Federal Court of Australia Act 1976* (Cth) s 53A.

44 Review of Business Taxation, *A Strong Foundation – Discussion Paper: Establishing Objectives, Principles and Processes* (1998), 120. Both New Zealand and the United States similarly found that disputes mainly arose through an audit under self-assessment: see, eg, Chapple, above n 30, 318.

45 Bentley, above n 35; Robert J Bryant, 'The Taxpayer's Perspective' (Paper presented at the 31st Victorian Taxation Convention: *Tax in the 1990s: Sink or Swim?*, Lorne, Victoria, 29–31 October 1992).

46 These internalised exchanges could be an 'informal dispute' or a 'dispute', depending upon how the terms are defined. Mining the ATO data for such statistical information is not possible without the ATO's support.

47 Chapple, above n 30, 319.

48 *Ibid* 313.

vary the decision.⁴⁹ The Tax Commissioner's decision can be regarded as being upheld outright, at least practically, in the case of decisions affirmed, dismissed and withdrawn.⁵⁰ The taxpayer's objection is upheld outright in the case of decisions set aside. If the AAT varies the decision, this means that the Tax Commissioner's decision has been changed or altered in some way. In this grey situation, neither the Tax Commissioner nor the taxpayer can claim full success, although, given that the onus is on the taxpayer to prove that the ATO's assessment is incorrect, this may be considered as a moral victory to the taxpayer.

In terms of structural organisation, the taxation division of the AAT is divided into the Taxation Appeals Division ('TAD') and the Small Taxation Claims Tribunal ('STCT'). These bodies differ substantially in terms of jurisdiction, application fee, confidentiality, conduct and timeliness. Given that the focus of this study is on administrative resolution of small tax disputes, it is worth elaborating on the STCT. The STCT is not a separate tribunal, but a part of the AAT. If the amount of tax in dispute is under \$5000, or if the ATO refuses the taxpayer's request to be released from a tax debt (any amount), then the taxpayer may elect to have the matter dealt with by the STCT. A decision of the STCT is a decision of the AAT, and thus is able to be appealed in accordance with the *AAT Act*.

There are some key differences between the AAT and the AAT in its role as the STCT:

- Application fee: The standard application fee payable to the AAT is currently \$777 per application (a reduced fee of \$100 is available in certain circumstances), while it is \$77 per application to the STCT. The application fee to the AAT is refundable in full if the decision is in favour to the taxpayer in any way, while the application fee to the STCT is not refundable.
- Confidentiality of the application: It is the taxpayer's prerogative to have the AAT hearing held in private,⁵¹ while the STCT will be in public unless the taxpayer can successfully demonstrate to the Tribunal why the hearing should be in private.⁵²
- Conduct: The STCT tends to conduct its proceedings with less formality and more expedition than the AAT. Data indicate a clear preference for STCT matters to be dealt with at conferences and teleconferences, rather than in a formal hearing.⁵³

49 *Taxation Administration Act* s 14ZZP.

50 Administrative Appeals Tribunal, *AAT Decisions: Understanding Your Decision, and What Happens Next* (2012).

51 Under the amended *Taxation Administration Act* s 14ZZE, the taxpayer can request the AAT hearing to be held in private.

52 *AAT Act* s 35.

53 Binh Tran-Nam and Michael Blissenden, 'Compliance Costs of Tax Dispute Resolution in Australia: An Exploratory Study' in Michael Walpole and Chris Evans (eds) *Tax Administration and the 21st Century* (Prospect Media, 2001) 296.

- Internal time line: In principle the AAT gives the ATO more time to provide section 37 (*AAT Act*) documents (35 days compared with the 14 days provided by the STCT). However, in practice, the ATO has found it difficult to meet that deadline.⁵⁴

In short, the operation of the STCT can be characterised as follows:⁵⁵

- Jurisdiction: The amount of tax in dispute is less than \$5000, or the ATO refuses the taxpayer's request to be released from paying a tax debt.
- Application: The taxpayer files a two-page application form to the AAT seeking the review of the ATO decision.
- Application fee: The standard fee is \$77 per application, and this fee can neither be reduced nor refunded.
- Process: Pre-trial conference before members of the AAT to discuss facts and issues (a second conference or mediation may also be called), then proceeding to STCT hearing.
- Type of hearing: Informal hearings held in public, unless the taxpayer can convince the STCT otherwise.
- Decision: Oral decision is made at the end of hearing, but written reasons are available within two months of hearing either upon request or if the AAT member(s) wants more time after the hearing to think about the decision.
- Time frame: The STCT aims to finalise the case within 12 weeks of the taxpayer lodging an application for review of decision (rarely met).
- Appeal rights: It is possible to appeal on a point of law to the Federal Court.
- Award of costs: No award of costs.
- Decision precedential: Non-precedential.

F The Courts

Tax disputes can only be ultimately resolved via judicial determination, as recently affirmed by the Hon Bill Shorten, Federal Assistant Treasurer: 'The ATO has sole responsibility for interpreting the taxation laws at first instance (for the purposes of administering those laws), while the Courts are the final arbiters'.⁵⁶

The Federal Court and ultimately the High Court have jurisdiction to finalise substantive tax disputes. Although state courts do not have jurisdiction to hear substantive tax disputes, they have jurisdiction in tax debt recovery disputes.

54 Ibid 297.

55 Andrew J Maples, 'Resolving Small Tax Disputes in New Zealand – Is There a Better Way?' (2011) 6(1) *Journal of the Australasian Tax Teachers Association* 96, 126–8.

56 Bill Shorten, 'Address to the Tax Forum' (Speech delivered at the Australian Tax Forum, Canberra, 5 October 2011).

The judicial route for resolving tax disputes is based on a variety of statutes:

- Part IVC of the *Taxation Administration Act*: challenging the ATO decision in the Federal Court;
- Part IVA of the *AAT Act*: appealing to the Federal Court from a decision of the AAT;
- *Administrative Decisions (Judicial Review) Act 1977* (Cth) (*'ADJR Act'*): applying for an ATO decision to be reviewed by the Federal Court; and
- *Judiciary Act 1903* (Cth) (*'Judiciary Act'*) and state and territory equivalent Acts: seeking an injunction, declaration or some kind of relief (relatively rarely used).⁵⁷

The apparent simplicity of this list masks an important distinction, between the nature and effect of seeking relief through the objection and appeal process provided under part IVC of the *Taxation Administration Act*, and the type of challenge available under either the *Judiciary Act* or *ADJR Act*. Section 39 of the *Judiciary Act* recognises an inherent right for any party whose interests are directly, materially and adversely affected by an administrative decision of the executive branch of government to seek review of that decision by the Federal Court of Australia.⁵⁸ The result of such an application would likely be a direction by the Federal Court to the administrative body concerned, to make the decision again in a manner that does not offend the applicant's rights to a fair decision: free of bias, irrelevant considerations, with regard to full relevant facts, and so on. A similar but more statutorily defined right exists under the *ADJR Act*,⁵⁹ to seek a review of the administrative decision concerned by the Federal Court, with similar effect. Since the decision of the High Court in *Federal Commissioner of Taxation v Futuris Corporation Ltd*,⁶⁰ however, it is clear that only deliberate maladministration by the Commissioner will found an application for review by the Federal Court or High Court. The indication by the High Court is that these remedies will only really be effective in cases 'of corruption and other deliberate maladministration';⁶¹ in other cases the most appropriate remedy is the part IVC procedure discussed below. An appeal within the part IVC process may proceed to the Federal Court (see below), but this is different to an application for judicial review directly to that court.

Part IVC of the *Taxation Administration Act* is, it would appear, the most appropriate procedure to be used to challenge an assessment.⁶² It applies where

57 Roshni Sheena Mookhey, 'Dispute Resolution in Tax' (2012) forthcoming *eJournal of Tax Research*.

58 A similar right is available to approach the High Court of Australia under *Constitution s 75*. Costs would tend to make Federal Court approaches more common.

59 The *Judiciary Act* remedy is sometimes used because it is wider and less statutorily constrained/defined than the *ADJR Act* remedy.

60 (2008) 237 CLR 146.

61 *Ibid* 167.

62 The twin operation of *ITAA 1936* ss 175 and 177 make it clear that an assessment may be challenged only via the pt IVC procedure. The judicial review process described above is available where it is alleged that maladministration has rendered the assessment invalid (and thus what is challenged is not an assessment), or in cases that do not involve an assessment but involve some other administrative act.

there has been an assessment that the taxpayer seeks to challenge. In these cases, the taxpayer must first object to the assessment, and then, if still dissatisfied with the ATO's objection decision, the taxpayer can appeal from the ATO decision or the AAT arbitration to the Federal Court. Unlike the AAT, the Federal Court is a judicial body, and is not able to re-examine the discretions of the ATO. Its role is to examine the legality of the decision-making process, so as to determine whether or not such discretions have been exercised in accordance with the law. Concepts such as relevant or irrelevant considerations are important in ascertaining whether the ATO has acted in an appropriate manner in exercising its discretions. The Federal Court can confirm or vary the decision,⁶³ and its adjudication is precedential. The taxpayer or the Commissioner of Taxation can then appeal against the Federal Court's decision to the full Federal Court, and, ultimately, to the High Court of Australia.

IV EFFECTIVE ACCESSIBILITY TO TAX JUSTICE

Part III demonstrates that Australia has a comprehensive and well-established system of tax dispute resolution. In particular, the external, independent process for resolving tax disputes offers both administrative arbitration and judicial adjudication. However, the mere existence of such a system or process alone does not guarantee that social justice is served. This is true if, for a number of reasons, taxpayers, especially individual taxpayers, may be unable to access administrative or judicial determination for resolving tax disputes. In this case, the system of tax dispute resolution can be considered to be ineffective.

It is well known that costs to individuals are a problem throughout the legal system, and can be a significant barrier to access to dispute resolution. As demonstrated below, these costs can be very substantial in the case of tax dispute resolution, whether measured in absolute terms or relative to the size of the amount of the tax in dispute. However, prior to discussing how such costs can be estimated, it seems worthwhile to make a few remarks.

First, although the process of tax dispute resolution is supposed to generate some benefits (such as clarity or certainty of tax laws thus serving the need of the rule of law that the law should be 'readily known and available, and certain and clear'⁶⁴), it is costly to the whole of society. In addition to taxpayers, the ATO, AAT and courts also incur costs in the process of tax dispute resolution.⁶⁵ For example, it has been estimated that the monetary costs to all relevant

63 *Taxation Administration Act* s 14ZZP.

64 See the Law Council of Australia's expression of one of the rule of law principles: Law Council of Australia, *Rule of Law* <<http://www.lawcouncil.asn.au/programs/international/rule-of-law.cfm>>. It is accepted that this is only one expression of the rule of law, and is arguably also (in the view of some) a limited/technical expression. A full discussion of the rule of law and its role in tax is beyond the scope of this article. The need for conformity of our law and legal institutions to liberal legal – and thus rule of law – principles seems, however, to be generally accepted in the Australian community, and is thus relied upon as an assumption underpinning the critique in this article.

65 The ATO spends about \$81 million per year on legal costs: Australian Taxation Office, above n 28, 3.

stakeholders in the matter of *Federal Commissioner of Taxation v Hart*⁶⁶ were about \$1.2 million (in 2006 price levels).⁶⁷ The costs to the ATO, the AAT and the court system are not relevant to the present paper, which is confined on the costs to taxpayers. In particular, the paper focuses on individual taxpayers to whom the question on access to tax justice is meaningful.

Second, a taxpayer who is in dispute with the ATO may incur costs at different stages of dispute resolution, which in principle can encompass both ADR and judicial determination. Since this article is primarily concerned with access to external review of tax disputes at the AAT level, its focus is on the costs incurred by taxpayers specifically at the AAT. Costs incurred at other stages, such as internal ATO review or court appeals, are ignored. Note, however, that adding the personal costs at other stages to those incurred at the AAT level would strengthen our central argument.

Third, the costs (excluding the tax debt) to taxpayers should be comprehensively defined, rather than confined to out of pocket expenses. They should include explicit costs, implicit costs and psychological costs. Explicit costs refer to monetary expenses incurred by the taxpayers, such as application fees or professional assistance fees. Implicit costs refer to the opportunity costs of time expended by the taxpayers and unpaid helpers in dealing with the resolution process. In the literature on tax compliance costs, researchers also recognise psychological costs, which in this case refer to the stress, frustration and anxiety that the taxpayer typically suffers as a result of disputing an ATO decision.⁶⁸

Fourth, data about actual costs should be, in principle, derived from a large-scale survey or in-depth interviews with taxpayers whose tax disputes with the ATO were finalised, whether by the ATO's internal review, the AAT or the courts. Such a study is in general not possible for a number of reasons, primarily because of the confidentiality of the tax dispute resolution process (so that it is not possible for independent researchers to identify a random sample of suitable participants without assistance from the ATO). In the absence of estimates of actual costs, the approach taken is to construct hypothetical costs under various scenarios based on information obtained from legal experts who have had experiences working with the ATO, the AAT and the courts.

A Explicit Costs (Monetary Expenses)

Monetary expenses incurred by the taxpayer arise from three separate sources: court and tribunal fees, professional advice and assistance costs, and personal expenses. There are a variety of court and tribunal fees, such as application fees (the Tribunal), filing fees (the courts), setting down fees (the

66 (2004) 217 CLR 216 ('Hart').

67 Justin Dabner, 'An Old Methodology in a New World: A Comment on Our Current System of Judicial Decision Making in Tax Cases' (2006) 2(1) *Journal of the Australasian Tax Teachers Association* 144, 150.

68 See, eg, Cedric T Sandford, Michael Godwin and Peter Hardwick, *Administrative and Compliance Costs of Taxation* (Fiscal Publications, 1989) 18.

Federal Court) and hearing and transcript fees (the courts). The full application fees to the STCT and the TAD are currently \$77 and \$777, respectively (the latter of which can be reduced to \$100 in certain circumstances). Note that the application fees have increased over time, at more or less the same rate as CPI inflation: from \$639 in 2006–07, to \$777 in 2010–11 at the TAD; and from \$64 in 2006–07, to \$77 in 2010–11 at the STCT.⁶⁹ It was estimated over a decade ago that for any taxpayer who may wish to go through the entire process from the Tribunal to a single judge of the Federal Court, then the Full Federal Court and finally, with special leave, to the High Court, the fees for these forums alone could approach \$10 000,⁷⁰ which corresponds to about \$15 000 in current prices.

However, the above fees represent, in many cases, only a very small fraction of the total cost of litigation. Professional advice and assistance costs, if incurred, would represent the bulk of the costs to taxpayers. Note that legal representation at the AAT is completely optional. In fact the STCT is designed for taxpayers to represent themselves. The vast majority of tax dispute cases do not proceed to a hearing at the AAT,⁷¹ and it is known that the proportion of self-represented taxpayers at a hearing is less than 50 per cent.⁷² It seems plausible to suggest that more than 50 per cent of taxpayers who are in dispute with the ATO would choose to represent themselves at the AAT conference, as applicants are more likely to employ professional assistance at a hearing than at a conference. Given the technical nature of taxation as discussed previously, it seems unwise for the taxpayer who is serious about his or her dispute with the ATO to proceed to a conference or hearing without the paid assistance of a qualified lawyer or accountant. Even at earlier stages of the process, it seems sensible for the taxpayer to employ the services of such an expert.⁷³ This is consistent with the fact that currently more than 70 per cent of Australian individual taxpayers rely on the services of tax agents for the completion and lodgement of their income tax returns.⁷⁴

The costs of professional advice and assistance depend on the hourly (or daily) rate and number of chargeable hours (or days). The market for tax-professional services, especially those of tax lawyers, is somewhat specialised. Not all lawyers or accountants can advise on tax matters. Based on the current market for legal and accounting services, it is estimated that a tax lawyer (or tax accountant) would normally charge at least \$2000 per day or \$300 per hour for

69 Based on information provided by the present AAT Registrar.

70 Tran-Nam and Blissenden, above n 53.

71 For example, in 2010–11, the percentages of applications finalised without a hearing at the TAD and the STCT were 85 per cent and 82 per cent, respectively: *AAT Annual Report 2010–11*, above n 37, 132.

72 According to information provided by Professor Robert Deutsch, currently Vice-President of the AAT, the broad rate of self-represented applicants is 50 per cent across the whole AAT, and the percentage is higher in non-tax matters than that in tax matters.

73 In 1996, taxpayers were represented in 66 out of 76 Tribunal reported cases: Chapple, above n 30, 326.

74 According to the ATO, 71 per cent of Australian individual taxpayers in 2009–10 used tax agents to assist with their income tax returns: Australian Taxation Office, *Taxation Statistics 2009–10* (2012) 12.

their professional assistance.⁷⁵ Note that these estimates are based on normal conditions, and that it is possible for taxpayers to obtain qualified advice at a lower cost.

It is conservatively estimated that a taxpayer who chooses to employ a lawyer or an accountant to attend a tax dispute case at the AAT would require about two days of professional assistance (including discussion, preparation, conference and hearing).⁷⁶ This would cost the taxpayer about \$4000. For a typical TAD case, it is suggested that the taxpayer would require three days of professional assistance, amounting to a sum of about \$6000. For the purposes of comparison, it is worthwhile to recall the Commonwealth Attorney-General's Department's 1992 estimate that a complex case at the AAT costs between \$30 000 and \$50 000, which is comparable to the cost of a Federal Court case.⁷⁷ The corresponding cost range in current prices would be about \$45 000 to \$75 000.

A final source of monetary costs is related to personal expenses. These cover transportation, telephone calls, postage stamps, and so on, arising from the tax dispute resolution process. On average, personal expenses relating to the application are estimated at \$200. This estimate does not include accommodation costs that may be incurred by taxpayers who do not reside in capital cities. The inclusion of accommodation costs will undoubtedly greatly increase the total amount of personal expenses.

There are of course some reliefs to taxpayers for monetary expenses incurred in tax dispute resolution. First, these expenses are recognised by the ATO as legitimate income tax deductions. Second, the full application fee to the TAD of the AAT is refundable if the application is successful. This fee can also be reduced to \$100 in certain circumstances, but the reduced fee cannot be refunded, regardless of the outcome of the application. Third, legal aid is also available to a limited category of eligible taxpayers. Further, the ATO is also willing to pay taxpayers' court costs in a small number of 'test' cases, in order to seek clarity in the law from the courts. Fourth, the courts award costs to successful applications by taxpayers (but there is no cost awarded by the AAT).

B Implicit Costs (Opportunity Costs of Time Losses)

Tax dispute resolution is a time consuming process to taxpayers and their unpaid helpers (if they have any). The taxpayer and unpaid helpers must spend time to learn about the process, file the application, prepare documents, search for professional assistance (if any), discuss with his or her legal/accounting advisor, travel, and appear before the Tribunal. Those who use a

75 This represents the rate of a junior barrister (based on interview with Professor John Glover of RMIT University who has from time to time represented both the ATO and individual taxpayers on different matters at the AAT and the Federal Court).

76 Based on information provided by Mr David Schabe, now a senior ATO officer, who used to work as a lawyer for the AAT in Brisbane, and Professor John Glover.

77 Attorney-General's Department (Cth), 'The Courts and the Conduct of Litigation' (Cost of Legal Services and Litigation Discussion Paper No 6, Submission to Senate Standing Committee on Legal and Constitutional Affairs, 5 March 1992) [2.32], [2.36].

lawyer/accountant spend more time with their advisers, but those who do not presumably must spend more time preparing for the case and learning about the process. Note that these opportunity costs are not recognised by the courts in awarding costs.

According to informed sources, it is likely that the taxpayer and unpaid helpers will have to spend an average of 48 hours filing applications, preparing documents, researching and discussing with their legal/accounting advisor and travelling. It is also estimated the taxpayer will have to spend, on average, 24 hours to appear before the STCT or the TAD.⁷⁸ This means an applicant to the TAD or STCT will have to spend, on average, about 72 hours on his or her application. Using an average after-tax average earning of \$25 an hour, this is equivalent to \$1800.

C Psychological Costs

Tax compliance activities are generally stressful. It seems plausible to suggest that tax dispute resolution and the associated tax audit are the two most stressful, because this process is directly adversarial. It is also argued that psychological costs can be very substantial, because of the lengthy duration of the resolution process (see Section D below), and the power asymmetry between the taxpayer and the ATO discussed previously. Psychological costs thus also act as a barrier to access to tax justice. However, to avoid unnecessary complications associated with valuation, psychological costs are excluded in this paper despite their theoretical relevance.⁷⁹

D Timeliness of Tax Dispute Resolution

Timeliness is an important factor in cost determination, and substantial delays in obtaining information from the ATO, conferences, mediations or hearings will increase the personal costs of tax dispute resolution to the taxpayer. Table 1A below reveals that tax disputes at the AAT's TAD generally take a long time to be finalised.

78 The figures for those time losses were based on an informal discussion with David Schabe. No distinction is made between the STCT and the TAD in terms of the taxpayer's time expended, because the AAT's experience is that 'applications dealt with in the Small Taxation Claims Tribunal cannot necessarily be completed faster than other types of taxation reviews': *AAT Annual Report 2010-11*, above n 37, 25.

79 Suffice it to say that an assessment of psychological costs has not yet been attempted in empirical studies of quantitative tax compliance costs. What limited research into the psychological costs of tax compliance has been conducted is basically qualitative: see, eg, Consuelo Díaz and Maria L Delgado, 'The Compliance Costs of Personal Income Taxation in Spain' in Cedric T Sandford (ed), *Tax Compliance Costs Measurement and Policy* (Fiscal Publications, 1995) 210, 225; Binh Tran-Nam and John Glover, 'Estimating the Transitional Compliance Costs of the GST in Australia: A Case Study Approach' (2002) 17 *Australian Tax Forum* 499; Robin Woellner, Cynthia Coleman, Margaret McKerchar, Michael Walpole and Julie Zetler, 'Can Simplified Legal Drafting Reduce the Psychological Costs of Tax Compliance? An Australian Perspective' [2007] (6) *British Tax Review* 717.

Table 1A: Percentage of Applications Finalised Within 12 Months at the AAT

	Target	2008–09	2009–10	2010–11
TAD	75	29	26	36
All AAT Jurisdictions	–	62	63	72

Source: Administrative Appeals Tribunal, Annual Report 2010–11 (2011) 24, table 3.9.

While there was a marked improvement in the proportion of applications finalised within 12 months of lodgement in the TAD in 2010–11, the actual proportions have consistently fallen short of the target of 75 per cent. It is also obvious that tax dispute cases take considerably longer than other dispute cases to be finalised by the AAT. In fact, only 54 per cent of tax dispute applications were finalised by the TAD within 18 months in 2010–11.⁸⁰ According to older data, in the late 1990s, the TAD of the AAT took, on average, about a year to finalise a case.⁸¹

The proportions of tax dispute cases finalised by the STCT have also fallen short of its aim of 12 weeks, as shown in Table 1B below.

Table 1B: Percentage of Applications Finalised Within 12 Weeks

	Target	2008–09	2009–10	2010–11
STCT	12 weeks	18	22	34

Source: Administrative Appeals Tribunal, Annual Report 2010–11 (2011) 25, table 3.10.

Tax dispute cases in the STCT are, in principle, expected to take less time to finalise than those in the TAD. However, in reality, as already mentioned,⁸² little time saving can be expected.

E Some Numerical Estimates of Costs

Now, gathering all quantitative estimates derived so far and assuming a personal marginal income tax rate of 30 per cent, Table 2 summarises the estimated average costs to the taxpayer at the AAT level under different assumptions about the use of professional advice and assistance (estimates have been rounded off).

80 *AAT Annual Report 2010–11*, above n 37, 24.

81 Tram-Nam and Blissenden, above n 53, 300.

82 See discussion in n 78 above.

Table 2: Estimated Average Costs (\$) of Tax Dispute Resolution at the AAT to the Taxpayer

	Without professional assistance	With professional assistance
TAD	2500	6700
STCT	2000	4800

* These estimates have been rounded. For example, $(1-30 \text{ per cent}) \times (777 + 200) + 1800 = \2484 (TAD, no professional assistance), rounded to \$2500; or $(1-30 \text{ per cent}) \times (77 + 4000 + 200) + 1800 = \4794 (STCT, with professional assistance), rounded to \$4800.

It is interesting to note that the estimated average personal costs to the taxpayer for resolving a tax dispute at the STCT are very close to the maximum amount of tax in dispute (currently \$5000). If the taxpayer chooses to represent himself or herself, then his or her personal costs will be more affordable, but his or her chance of being successful will be negatively impacted. While no numerical estimate of the average cost to the taxpayer at the court level has been attempted, it seems sensible to suggest that such an average cost will be substantially higher than that at the AAT level (as presented in Table 2).

F Evidence of Ineffective Accessibility

The hypothetical cost scenarios in Table 2 confirm that costs of tax dispute resolution, even at the STCT, can be substantial to the taxpayer, especially if he or she chooses to engage professional assistance. At a theoretical level, it is plausible to argue that high costs deter taxpayers from seeking external review of ATO decisions. But is there any concrete empirical evidence to support this hypothesis?

To obtain a direct answer to the above question, a researcher needs to survey those taxpayers who were in dispute with the ATO. As discussed previously, such a survey is not possible, primarily because of the confidential nature of tax disputes. More specifically, without the ATO's assistance, it would not be possible to obtain a random sample of such individuals. An alternative primary data collection approach would be to undertake limited interviews with clients of accounting/legal firms who have been in dispute with the ATO. While such interviews would be very useful, this approach also requires support of the study by the firms and permission from their clients.⁸³ In the absence of such survey/interview results, the only alternative approach is to examine aggregate statistics published by the ATO and the AAT, and to infer the possible impact of costs on actual accessibility from these data. A quick examination of these statistics suggests that high costs to taxpayers serve as effective barriers to access to the legal system for resolving tax disputes.

83 The process of requesting such support and permission is too time consuming, and we cannot afford such time losses given our tight constraints. However, we would certainly try to do so in any future studies on this topic.

According to the latest statistics published by the ATO, 97 per cent of tax and superannuation objections made in 2010–11 were finalised at the objection stage.⁸⁴ This means that only three per cent of taxpayers sought independent review of the ATO's decisions. An overwhelming proportion (80 per cent) of such taxpayers chose the AAT to litigate their disputes.⁸⁵ Even though only a small fraction of taxpayers proceed to the courts, taxation law is still currently the third most litigated area of the law in Australia.⁸⁶ It is suggested that the percentage of taxpayers seeking external review (three per cent) is very low, and does not seem to reflect taxpayers' true preferences. It seems reasonable to assume that a much higher percentage of taxpayers in dispute with the ATO would like to resolve their matters by external review. A primary reason for this low percentage of applications to AAT review must arguably be the high costs (and long duration) discussed earlier. This seems to be consistent with the fact that, in 2010–11, about two thirds of taxpayers seeking independent review of the ATO decision chose not to proceed to a formal hearing,⁸⁷ possibly because of their greater awareness of the costs and time involved after formally seeking review.

Two points deserve mention. First, the above three per cent included both corporate and individual taxpayers. However, it seems reasonable to claim that corporate taxpayers are more likely to seek external review of the ATO decision than individuals. Under this assumption, if we exclude corporate taxpayers, then the percentage of individual taxpayers seeking external review would be definitely lower than three per cent. Second, it is conceivable that many taxpayers choose to proceed to external review of ATO decisions for motives other than short-term financial gain. If we exclude these taxpayers from our consideration, then the impact of costs on access to procedural justice would be even more pronounced.

As a final piece of evidence, we will consider the role of the STCT within the AAT over time. According to data published by the AAT, the STCT currently plays a minor role relative to the TAD. For example, in 2010–11, only about six per cent [= 73 / (73 + 1103)] of all tax dispute applications lodged at the AAT went to the STCT.⁸⁸ This was not the case more than a decade ago. For example, in 1997–98 and 1998–99, almost 25 per cent [= 311 / (311 + 949)] and more than 31 per cent [= 357 / (357 + 768)] of tax dispute cases of the AAT went to the STCT, respectively.⁸⁹

The remarkable declining role of the STCT, both in absolute and relative terms, is attributable to a variety of factors. These include:

84 Australian Taxation Office, above n 28, 3.

85 Ibid.

86 Behind corporation law and consumer law: see Federal Court of Australia, *Annual Report 2010–2011* (2011) 27.

87 This is deduced from the facts that 97 per cent tax disputes were finalised by the ATO internal review process and another two per cent were finalised prior to hearing: Australian Taxation Office, above n 28, 3.

88 *AAT Annual Report 2010–11*, above n 37, 21.

89 Administrative Appeals Tribunal, *Annual Report 1998–99* (1999) 99.

- the cumulative effect of inflation and economic growth, the result of which has been that the upper eligibility limit of \$5000 has become proportionally smaller and smaller over the years;
- the high costs of small tax disputes; and
- the fact that some taxpayers may be aware that they have a low chance of success in the STCT.

In fact, the decline of the STCT is not surprising in view of Table 2. Whatever the reasons, the declining role of the STCT indicates a gradual decline of effective accessibility to procedural justice for the resolution of small tax disputes.

To summarise, the high costs of tax dispute resolution to the taxpayer act as a significant barrier to access, reducing the effective accessibility of the external tax dispute resolution process. Clearly, the costs of tax disputes to personal taxpayers vary widely depending on the nature of the disputes. It seems plausible, however, to assume that the costs are 'regressive' in relation to the amount of tax in dispute; that is, the costs as a percentage of the taxes in dispute will decline as the amount of tax in dispute increases. Similarly, it seems plausible to assume that the costs are also regressive in relation to the income of the taxpayer; that is, the costs as a percentage of the taxpayer's income will decline as the income of taxpayer increases.

V IMPACT OF INACCESSIBILITY

In the previous section of this article we have suggested that the high costs associated with tax disputes have the effect of making it not worthwhile for individual taxpayers to take matters beyond the ATO's internal decision-making process. This makes the system of tax dispute resolution in Australia effectively inaccessible, in the sense that many individual taxpayers who dispute with the ATO will either not reveal themselves, or not take the disputes to the external review stage, despite its theoretical availability. What are the implications, particularly the social justice implications, of this inaccessibility?

To assess the social dimensions of ineffective accessibility of an essential government service, it would be helpful to place it in the broader context of socioeconomic changes in Australia, especially over the past 30 years. As a young nation with a rather humble beginning, the notion of a 'fair go' has been enshrined in the Australian ethos. Many Australians like to think of themselves as egalitarians. As late as 1967, Prime Minister Harold Holt proudly claimed that he knew of no other free country where 'what is produced by the community is more fairly and evenly distributed among the community' than it was in Australia.⁹⁰ More recently, in his 1998 election victory speech, Prime Minister

90 Quoted in Peter Whiteford, 'Are the Rich Getting Richer and the Poor Getting Poorer?' (28 September 2001) Inside Story <<http://inside.org.au/are-the-rich-getting-richer-and-the-poor-getting-poorer>>.

John Howard expressed to his intention to maintain Australia's traditional values, including mateship and egalitarianism.⁹¹

While data were limited, there does appear to have been a substantial long-term decline in income inequality between the 1940s and the 1970s in Australia.⁹² However, this trend has been reversed since the 1980s, perhaps due to Australia's market liberalisation and globalisation policy, which was commenced by the Labor Government in the mid-1980s and further consolidated and extended by the Liberal Government from the mid-1990s onwards. The results of the pro-market policy have been highly beneficial in terms of economic prosperity and rising average incomes. Unfortunately, this positive aggregate growth has been associated with rising income inequality. Better and more readily available data produced by the Australian Bureau of Statistics demonstrate that the Gini index of income inequality⁹³ has increased from 0.27 in 1981–82 to 0.328 in 2009–10.⁹⁴ Similarly, a recent study commissioned by the Australian Council of Trade Unions shows that the distribution of wealth in Australia is much more unequal than people think, and that Australians favour a more equal wealth distribution.⁹⁵

Lack of access to independent tax dispute resolution has two aspects: an absolute (direct) impact, and a relative (indirect) one. The absolute impact refers to the inability to access an essential government service, which represents a violation of social justice according to the definition proffered at the beginning of the article. The relative impact is related to distributive justice. It seems plausible to assume that access to external review of tax disputes is income-related, in the sense that high-income taxpayers tend to access external review of tax disputes more often than low-income taxpayers. If one is willing to entertain this assumption, then an obvious negative consequence of inequality of income distribution is inequality of access to government services. The twin inequalities of income and access to government services undermine egalitarianism, a notion that many Australians continue to value.

A second impact of ineffective accessibility is concerned with the relationship between procedural tax justice, taxpayer morale and voluntary tax compliance. Tax compliance, voluntary or otherwise, is fundamental to the success of any modern tax system. Voluntary compliance is always greatly valued, as it would lower the operational costs of the tax system as a whole. According to the modern theory of tax compliance, one determinant of voluntary

91 Tom Conley, 'Globalisation and Rising Inequality in Australia: Is Increasing Inequality Inevitable in Australia?' (Paper presented at the Australasian Political Studies Association Conference, University of Adelaide, 2004) 1.

92 Whiteford, above n 90. Whiteford is referring to work of other economists.

93 The Gini index is the most commonly used summary measure of inequality, which varies from 0 (absolute equality) to 1 (absolute inequality).

94 Whiteford, above n 90, chart 1.

95 David Neal et al, 'Australian Attitudes Towards Wealth Inequality and the Minimum Wage: A National Survey of Knowledge, Attitudes and Perceptions of Wealth Inequality and the Minimum Wage' (Report prepared for the Australian Council of Trade Unions, 15 April 2011) <<http://www.actu.org.au/Images/Dynamic/attachments/7474/ACTU-Report-Inequality-and-Minimum-Wage.pdf>>.

tax compliance is tax morale, which can be defined as the intrinsic motivation to pay taxes, that is, the willingness to comply voluntarily. Tax morale, a term first introduced in 1969 by Strümpel,⁹⁶ in turn depends on social norms, tax fairness, governance and trust and taxpaying culture.⁹⁷

A literature review by Wallschutzky⁹⁸ reveals that motivations for tax evasion include perceptions of high tax rates,⁹⁹ government profligacy with tax revenue,¹⁰⁰ and an overly coercive tax administration.¹⁰¹ Fairness perceptions in tax include fair treatment of taxpayers (procedural fairness), as well as fairness as to who is paying tax (policy fairness). We argue that fairness and even-handedness by the tax authority are essential to encourage integrity amongst taxpayers, and that a dimension of this fairness is lost if taxpayers cannot appeal against a decision or have that decision reviewed by an independent party. Our previous argument also implies that if taxpayers perceive that only wealthier taxpayers can afford to challenge the ATO in the AAT or the courts, this will have a negative impact on their perception of fairness.

Wallschutzky's work with known tax evaders emphasises taxpayer dissatisfaction with their treatment by the ATO as a possible 'important influence on future levels of tax evasion'.¹⁰² Difficult though it may be to implement, Wallschutzky's work implies that even tax evaders must be fairly treated as a means of ensuring that they do not evade again. It is suggested that there is even greater justification for fair and generous treatment of taxpayers who are not evaders. Wenzel has also identified a significant role for perceptions of fairness in encouraging taxpayer cooperation with the tax system.¹⁰³ Meanwhile, Braithwaite and Reinhart¹⁰⁴ (as is mentioned by Wenzel) saw a more cooperative attitude on the part of taxpayers where they were made aware of the Taxpayers' Charter, including their ability to make complaints and appeal decisions.

96 See Burkhard Strümpel, 'The Contribution of Survey Research to Public Finance' in Alan T Peacock (ed) *Quantitative Analysis in Public Finance* (Praeger, 1969) 13.

97 See, eg, Benno Torgler, *Tax Compliance and Tax Morale: A Theoretical and Empirical Analysis* (Edward Elgar, 2007); Jeff Pope and Margaret McKerchar, 'Understanding Tax Morale and Its Effect on Individual Taxpayer Compliance' [2011] *British Tax Review* 587, 592.

98 This discussion of Wallschutzky's work has been based on Michael Walpole, 'Ethics and Integrity in Tax Administration' [2009] (33) *University of New South Wales Faculty of Law Research Series*, 12–13.

99 I G Wallschutzky, 'Possible Causes of Tax Evasion' (1984) 5 *Journal of Economic Psychology* 371, 374, citing Peter Dean, Tony Kennan and Fiona Kenney, 'Taxpayers' Attitudes to Income Tax Evasion: An Empirical Study' [1980] *British Tax Review* 28.

100 Dean, Keenan and Kenney, above n 99, 43.

101 Wallschutzky, above n 99, citing Günter Schmolders, 'Survey Research in Public Finance: A Behavioural Approach to Fiscal Policy' (1970) 25 *Public Finance* 300; Michael W Spicer and S B Lundstedt, 'Understanding Tax Evasion' (1976) 31 *Public Finance* 295; Max Frank and Danièle Dekeyser-Meulders, 'A Tax Discrepancy Coefficient Resulting from Tax Evasion or Tax Expenditures' (1977) 8 *Journal of Public Economics* 67.

102 Wallschutzky, above n 99, 383.

103 Michael Wenzel, 'Tax Compliance and the Psychology of Justice: Mapping the Field' in Valerie Braithwaite (ed) *Taxing Democracy: Understanding Tax Avoidance and Evasion* (Ashgate, 2003) 41.

104 Valerie Braithwaite and Monika Reinhart, 'The Taxpayers' Charter: Does the Australian Taxation Office Comply and Who Benefits?' (Working Paper No 1, Centre for Tax System Integrity, The Australian National University, December 2000).

The Australian experiences in the context of taxation are consistent with the findings of the ‘attitudinal’ model of compliance. That model emphasises the importance of an authority’s trustworthiness, the respectful treatment of people by the authority, and neutrality of procedure.¹⁰⁵ Two central arguments of this school of thought are: (a) that people comply with the law if they believe that the authority is legitimate and the law moral, not because they fear punishment; and (b) that public views of the authority’s legitimacy are related to judgments about the fairness of the procedure through which it makes decisions.¹⁰⁶ An implication is that people’s motivation for compliance extends beyond their concern for favourable outcomes, so long as they regard the authority as legitimate. Opponents of the procedural justice approach have indicated that people care more about a favourable outcome, and less about fairness, when the stakes (for example, the amount of tax in dispute) are high. There is insufficient empirical evidence at this stage to settle this disagreement.

In short, affordable access to independent review of an ATO decision is highly desirable, for the effect it will have on voluntary compliance and the integrity of the tax system. It is important to note that ease of access by taxpayers to external dispute resolution will not only promote a more cooperative culture between taxpayers and the ATO, but also a healthier working relationship between tax practitioners and the ATO. Given the high degree of taxpayers’ reliance on tax advisers in Australia, it would yield a double dividend to the administration of the tax system.

On the one hand, it may be said that if the amount in dispute is not worth fighting over, then there is little harm in removing such disputes from the formal resolution process. This is particularly so in light of the cost to society of such dispute resolution processes. It cannot be pretended that the fees set for the AAT, and more particularly the STCT, recoup anything approaching the costs to the government of operating these dispute resolution mechanisms. But the cost to the administration (and indeed to society) of a situation in which taxpayers might perceive themselves to be without recourse to fair adjudication may do more harm than is realised, because a sense of unfairness can undermine the community’s faith in the tax system.

Third, from the broad legal perspective, ineffective accessibility to independent tax dispute resolution also gives rise to the problem of the self-represented litigant (a person who conducts his or her case without professional representation). This is quite likely in tax dispute cases in view of the costs of professional assistance discussed in Part IV. Because of the technical nature of tax law, self-represented litigants are unlikely to be able to do justice to their cases unless they possess considerable tax expertise themselves. This remains true even in the presence of the support provided to self-represented litigants,

105 See, eg. Tom M Tyler, *Why People Obey the Law* (Yale University Press, 1990); Murphy, above n 6; Erich Kirchler, *The Economic Psychology of Tax Behaviour* (Cambridge University Press, 2007).

106 Tom R Tyler, ‘Procedural Fairness and Compliance with the Law’ (1997) 133 *Swiss Journal of Economics and Statistics* 219, 219.

such as the AAT's Outreach program.¹⁰⁷ In fact, it has been argued that 'the court's capacity to discharge its societal function is impaired when it engages with the self-represented litigant, thus preventing strict compliance with the rule of law'.¹⁰⁸ According to this line of reasoning, the self-represented litigant can be viewed as a challenge to justice.

A fourth and final impact of the inaccessibility of access is concerned with clarity of tax law. It is important to recall that one positive outcome of tax dispute resolution is the improvement in the clarity of the law itself. However, if access to external tax review is income-related, as we have been arguing, then it is conceivable that actual tax disputes centre on issues relevant to high-income taxpayers (for example, tax planning schemes), at the expense of tax issues more relevant to low-income taxpayers. The uneven distribution of areas of tax law uncertainty that are being clarified by the Tribunal and the courts is not a healthy development for tax law in the long run, and threatens the principle that all should have access to the legal system irrespective of their economic power.¹⁰⁹

We have so far refrained from discussing an alternative interpretation of tax justice in terms of the 'right' result, since this is not the focus of our article. The correctness, or otherwise, of the outcome of the process is nevertheless important and needs to be discussed, however briefly. The resolution of a tax dispute by the court system is expected to bring some benefits, such as clarity or certainty of the law. Unfortunately, many High Court decisions (for example, *Hepples*, *Federal Commissioner of Taxation v Orica Ltd*,¹¹⁰ *Federal Commissioner of Taxation v Montgomery*¹¹¹ and *Hart*) have been met with 'disappointment, critical disclaim and the identification of further grey areas and difficulties'.¹¹² Some legal scholars have argued that the inability of the courts in providing clarity and certainty to the tax law reflects the limitations of the literalist and purposive approaches to legal interpretation.¹¹³

VI CONCLUSIONS AND RECOMMENDATIONS

In this article, we have examined the relationship between independent tax dispute resolution and social justice in Australia. As background, it was first argued that tax disputes are different from other disputes in several fundamental respects, and thus warrant separate examination. We then provided an overview

107 The Outreach program explains the AAT's practices, procedures and processes to self-represented litigants. Further assistance, such as 'free' legal representation, may be available if the taxpayer makes a successful application for legal aid: *AAT Annual Report 2010-11*, above n 37, 14-15.

108 Richard Stewart, 'The Self-Represented Litigant: A Challenge to Justice' (2011) 20 *Journal of Judicial Administration* 146, 146.

109 Law Council of Australia, above n 64.

110 (1998) 194 CLR 500.

111 (1999) 198 CLR 639.

112 Dabner, above n 67, 144.

113 See, eg, Mark Burton, 'The Rhetoric of Taxation Interpretation and the Definition of "Taxpayer" for the Purposes of Part IVA' (2005) 18 *Revenue Law Journal* 4, 6-7.

of the current process of tax dispute resolution in Australia. In Part IV, we considered the personal costs of tax dispute resolution to the taxpayer under different plausible hypothetical scenarios. It is argued that the personal costs of tax disputes are sufficiently high, particularly in the case of small tax disputes, to deter individual taxpayers from seeking external scrutiny of the ATO's decisions. In the next Part, the impact of this ineffective accessibility was examined. In particular, it was argued that this gives rise to an inequality of access to government services that, together with rising income equality, undermines Australia's traditional value of egalitarianism.

The quantification of the hypothetical costs incurred by the taxpayer in seeking external review confirmed the existing knowledge that costs can be a considerable barrier to access to the legal system, especially if professional assistance is employed. This is perhaps more severe in the case of tax disputes, for a number of reasons. First, tax disputes tend to take longer to be finalised than other types of disputes. Second, tax law is a specialised area, and it can be costly to employ the service of a suitably qualified tax lawyer or accountant. Third, if the taxpayer chooses to go to the Tribunal or a court, the onus is upon him or her to show that the ATO decision is incorrect.

If the taxpayer decides to represent himself or herself, then the costs to the taxpayer are more affordable, and mainly take the form of implicit costs (value of time losses). However, given the technical nature of tax laws, all other things being equal, the taxpayer has a much poorer chance of success than if he or she employed the professional assistance of a lawyer or an accountant. In this case, inadequate representation also acts as an effective barrier to tax justice in the same way that the costs of professional assistance do. Note that, despite their selectivity, the test case litigation program and the availability of legal aid jointly serve to lower, to some limited extent, the barriers to access to tax justice.

The theoretical argument about access to tax justice is borne out by empirical data, which indicate that only a very small fraction (about three per cent) of taxpayers (including corporate taxpayers) who are in dispute with the ATO choose to seek external review. This has been accompanied by the markedly declining role of the STCT within the AAT over the last 12 years. These findings in turn imply that the independent review system, despite being operational, is not effectively accessible.

The findings in this article may pose a challenge to the tax authority in particular and the government in general. On the one hand, it is desirable that frivolous or vexatious tax disputes do not proceed to external review. On the other hand, genuine tax grievances should be heard by the Tribunal and the courts. It is an immensely difficult task to find an 'appropriate' level of application fees and assistance to the taxpayer that discourages frivolous but not genuine objection applications. A few immediate solutions seem to be within the control of the government. As expected, these solutions typically involve trade-offs; that is to say, greater social justice can only be obtained at certain costs to the government. A number of alternative recommendations are proposed in terms of the increasing level of costs to the government as follows.

It is apparent that the maximum threshold of the amount of tax in dispute falling under the jurisdiction of the STCT is too low. This threshold has remained at \$5000 for two decades, despite continuous inflation, as well as growth of income and taxation revenue, in the Australian economy during the same period. Thus, a simple and modest proposal would be to raise this threshold to, say, \$10 000 or \$15 000. Such an increase, if implemented, may reverse the declining role of the STCT within the AAT.

A substantially more radical proposal is to consider the asymmetry of resources between the ATO and the individual taxpayer. Given this asymmetry, a case can be made for a new procedure, which awards explicit costs to the taxpayer (including legal costs in particular) if his or her application is successful, but not to the ATO if the taxpayer's application is unsuccessful. An alternative to this proposal would be to reverse the onus for small tax disputes. Under this approach, for tax disputes under \$10 000 or \$15 000, the burden of proof would rest with the Tax Commissioner to demonstrate that his or her assessment is correct to the AAT or the courts. Perhaps these proposals could contribute in some way to improving taxpayers' accessibility to external review, making the legal system more effective, albeit at a cost to the government.

An even more radical and costly approach would be to make the ATO's internal review process more independent and accessible to taxpayers. A model that Australia could consider to adopt (and adapt) is the National Taxpayer Advocate ('NTA') of the Internal Revenue Service ('IRS') of the United States.¹¹⁴ Under this model, the Head of the NTA is directly appointed by the United States federal government, and is a member of the senior management team in the IRS, with access to high-level information flow. While the NTA is housed within the IRS and its operating budget forms a part of the IRS's budget, the NTA nevertheless operates independently of the IRS, in that it is not directly accountable to it but rather reports to Congress. Amongst other things, the Taxpayer Advocate Service conducts Low Income Taxpayer Clinics, which provide professional representation to individuals who need to resolve tax problems with the IRS. This seems to make the tax dispute resolution process more accessible to American taxpayers, especially those individuals on low incomes.

A completely different approach would be to treat the problem at its source, that is, to prevent the problem from occurring. Taxation is one area where many individuals are required to engage with the government on a regular basis. It might therefore be argued that tax disputes ought to be minimised as far as possible. This approach can be defended on both efficiency grounds (in terms of minimising the operating costs of the tax system), and the legitimisation of the government (as discussed in the previous section). Naturally, the practical implementation of such an approach through education, persuasion and so on, should be subjected to the conventional cost-benefit test.

114 Internal Revenue Service, United States Department of the Treasury, *The Taxpayer Advocate Service Is Your Voice at the IRS!* (12 June 2012) <<http://www.irs.gov/advocate/article/0,,id=212313,00.html>>.