# Submission
# Improving tax compliance - enhanced third party reporting, pre-filling and data matching

## Introduction and summary

Anonymous is concerned to express independent views on the workability of the proposed measure, and point out what relevant considerations are missing from the discussion paper.

Our submission can be summarised as follows:

- all third-party reporting should be consolidated into one legislative framework; these laws are easy to write and tend to proliferate in the absence of discipline; consolidation will help you sell this particular roll of red tape to the business community;
- the measure erodes the secrecy of the TFN by making it commonplace to give it to everybody;
- it may be difficult to write legislation that targets merchant credit and debit services, and so it may be appropriate to let the ATO explicitly nominate specific reporting entities;
- the measure is a comprehensive economic surveillance network for criminal law enforcement as well as tax administration, co-opting the private sector to spy on every taxpayer in Australia for the benefit of the Commonwealth; it should be overtly explained to the public and Parliament as such;
- the measure quietly side-steps the existing governance and oversight associated with the Guidelines for the Use of Data-Matching in Commonwealth Administration;
- it is inappropriate to impose penalties for technical breaches of the third-party reporting regime; penalties should be reserved for intentional non-compliance or reckless non-compliance that actually results in a loss to the Commonwealth; the Commissioner should be able to apply to a Court for an injunction to obtain compliance with the reporting regime;
- the Commissioner should, at least in practice, accept the data that the reporting entity has and not strictly enforce the power to specify a data format and medium;
- the Commonwealth should bear any additional costs imposed on reporting entities, since it is the Commonwealth that wants the data for a Commonwealth purpose.

## Consolidate third-party reporting as much as possible

The following regimes require entities to report information to the Commonwealth to assist the Commonwealth in enforcing laws in relation to other entities:

- annual investment income reports and TFN reports (Income Tax Assessment Act 1936, section 202D, regulation 56, who knows where the authority for that came from)
- reportable payments (Taxation Administration Act 1953, Schedule 1, Division 410)
- Pay As You Go Withholding (yes, it’s primarily cash withholding, but it’s also about information, especially since you use it to force payees to provide TFNs and ABNs)
- Tax File Number (‘TFN’) declarations
- Trust reporting in relation to beneficiaries (income tax return distribution schedule; also something about ultimate beneficiaries tax and TFN withholding -- the fact that we can’t readily understand all the overlapping schemes with confusing names in five different Acts is evidence that you need to consolidate)

- US FATCA
- OECD CRS
- Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (even though you don't require customer due diligence information to be reported up-front, you still require it to be collected into convenient places like banks so that you can hoover it up later)
- Australian Securities and Investments Commission (in relation to changes in share structure and owners)

There are many more.

It is one thing to make a person fill in a tax return or provide documentation when claiming a grant. It is another thing to make them report on other people. Consolidate this nonsense.

The principles on page 13 of the discussion paper are beautiful. Find any legislation, tax or otherwise, that can fit into that pattern, and consolidate it into this measure.

Reporting legislation is easy to write. With no brainpower, you can spend an hour and write a not-quite-identical clone of Division 410 and say "Yeah, enhanced third-party reporting" on your resume. Therefore they tend to proliferate. You should resist this impulse. Consolidate.

Tax legislation is garbage because nobody ever analyses the existing pile of legislation and condenses it down to the same meaning but knitted together more neatly (you tried with the ITAA97, but you gave up, and even then you cheated with section 1-3 i.e. "Jk, this Act has no meaning, read the other one instead hurr durr") .

## The measure erodes the secrecy of the TFN by making it commonplace to give it to everybody

You love matching on TFNs and unique numeric identifiers are fantastic. The problem is that for some unknown reason you decided to make the unique identifier also serve as a shared secret. You have an identifier that cannot be widely used to identify the taxpayer.

People are used to quoting their TFN to banks and employers. That is how people harvest their identities to rip you off on GST refund fraud, but you keep a bit of a lid on it by telling people "Only give it to banks, super funds and employers, nobody else!" Well now this measure says "Give it to your real estate agent, your company, your local council". You intend to expand this further in future. People don't read legislation, they'll only get the gist, you'll need to run a marketing campaign saying "It's OK to give your TFN to your real estate agent, x, y, but nobody else!"

We recommend that you stop using the TFN as a shared secret. No other system on Earth uses one arbitrary number as both username and password. Imagine if you had to wait 28-56 days to change your password for your email account. Hardly 21st century service. The TFN is a file number, a numeric identifier. If you want a numeric secret, then start issuing numeric secrets. Then you can use TFNs the way you should, which is the same as ABNs, as a convenient unique numeric identifier for a tax entity.

## Difficult of writing legislation that targets merchant credit and debit services

It may be difficult to write legislation that targets the Australian-based components of various payment systems, such as credit card networks, Paypal-like services, and whatever else merchants start using to get paid. For example, if you wrote this reporting regime 10 years ago, would you have captured Paypal? Would you have inadvertently captured KickStarter?

The difficulty will be ensuring that, for each type of service, you capture data from exactly one reporting entity for every transaction. You do not want to miss anything, and you do not want to impose on industry by collecting duplicates.

The usual approach would be to write detailed, convoluted legislation defining, or delegating a regulation-making power (to allow the creation detailed, convoluted regulations). As with substantive tax legislation, people will find schemes that step around the legislative definitions. The ATO will be forever crying to Treasury for amendments to keep it up to date.

On the other side of the fence, entities will have to waste time and money working out whether they fall under the legislation, and what obligations they have. This would be a particular burden for innovative start-ups with new service offerings. Such a system would necessarily result in reporting entities seeking binding rulings from the ATO, a burden on everybody.

Instead, the legislation should define the merchant credit and debit services industry broadly, and empower the ATO to issue a notice to a specific entity in that industry to report payments it processes for merchants. Therefore, reporting obligations would only arise after the ATO had advised a specific entity that reporting was required. This would allow the ATO to specify what classes of transactions it wanted reported, so that the overall system could target all payments exactly once, with no overlaps or gaps.

The ATO's ability to identify potential reporting entities should be backed by a simple obligation on every entity in the merchant debit and credit services industry to advise the ATO that they exist in that industry. This would be a small burden, simply lodging an electronic form. There would be next to no negative consequence for erring on the side of notifying the ATO of your existence rather than not. It would then be up to the ATO to work out whether they want you to report anything.

This approach, of delegating the selection of entities to administrative discretion, is usually not acceptable for imposing burdens on persons. For example, you would never get away with imposing taxation broadly and then letting the ATO, in its administrative discretion, decide who pays tax. However, the particular nature of the merchant credit and debit services industry mandates a flexible approach.

The decision to nominate an entity to report payments in the merchant credit and debit services industry should not be subject to merits review (e.g. Part IVC objection). It should be subject to judicial review where the ATO oversteps its jurisdiction (e.g. the entity simply does not process merchant credit and debit payments). The Commonwealth Ombudsman should monitor the selection of reporting entities to ensure that it is fair and results in the most efficient collection of the information required.

## Economic surveillance network for criminal law enforcement

The only time the discussion paper mentions "privacy" is in the context of the privacy of the TFN. And

this is a furphy, because the secrecy of TFNs is solely for the administrative convenience and loss mitigation of the ATO. The privacy or otherwise of a taxpayer's TFN is no skin off their nose, except to the extent that if someone defrauds the ATO using the TFN then the ATO will thrash around brainlessly for several months and refuse to deal with the taxpayer.

If you are going to impose an economy-wide financial surveillance network, you should be up-front about it. People (and Parliament) will accept or reject it on its terms.

If, however, you try to slip it past them with a boring discussion paper that omits this key issue, then you are only asking for trouble later when someone realises "Hey, they wrote an Act that lets the Commissioner issue regulations to monitor, well, anything."

The privacy implications of the measure are exacerbated by the ATO's practice of handing information over to law enforcement agencies. Dissemination to law enforcement is currently limited to serious offences and taskforces, but the vague terms of the National Anti-Gang Taskforce and the steady accumulation of similarly-broad taskforces means that more and more information will be shared.

Therefore the measure is not only a tax administration measure, it is a law enforcement intelligence-gathering measure.

Beyond law enforcement, the current push toward automatic international exchange of information means that the data gathered under the proposed measure will probably make its way to tax authorities and law enforcement agencies in other countries too. None of this is mentioned in the discussion paper.

## Side-stepping existing Privacy Commissioner oversight for data-matching

The ATO current observes a distinction between "legislative" and "non-legislative" data for data-matching. "Legislative" data is information like the contents of tax returns which, under tax law, flow into the ATO. "Non-legislative" data refers to bulk information that the ATO goes out and acquires, such as the massive database of every property transaction since 1990, the list of every motor vehicle purchased last year, and the list of every business that made a sale via credit card (and the amount).

Under the current Guidelines for the Use of Data-Matching in Commonwealth Administration, issued by the Privacy Commissioner, non-legislative data is subject to stringent controls. Before acquiring bulk data, the ATO must publish a data-matching protocol stating the purpose of the acquisition, how it will be used, and when the acquired data will be destroyed. The ATO must obtain the special dispensation of the Privacy Commissioner to depart from the guidelines, for example by keeping the

Under the current Guidelines, the ATO is generally prohibited from sharing bulk non-legislative data with law enforcement. This makes sense, because Parliament deliberately never gave law enforcement agencies the power to trawl entire private-sector databases on the off chance that something might look suspicious. This is a power we currently consciously withhold from criminal law enforcement agencies, because it is unhinged from any judicial oversight and, combined with the ability to arrest and prosecute, magnifies the risks associated with breach of privacy and misinterpretation of third-party data. The proposed measure quietly grants law enforcement the power to trawl confidential data sources without a

warrant, through the mechanism of the ATO.

In other words: currently, if a police officer wants to get the financial details for Joe Bloggs such as banking transactions, he gets a warrant from a magistrate. Under the proposed measure, the police officer would call up the ATO and ask for the information -- no judicial oversight.

If you intend to give police the ability to call up confidential information from private-sector databases with no judicial oversight, then you should do so overtly, by giving them that explicit power. Instead, the proposed measure provides that power through the back door, by way of third-party reporting to the ATO coupled with the ATO's information disclosure provisions.

The proposed measure quietly re-classifies the ATO's bulk data acquisition and data-matching from "non-legislative" data to "legislative" data, thus sweeping away existing controls over the use and on-disclosure of the acquired information.

The Australian Law Reform Commission, in reports 108 and 112, declined to recommend that the voluntary Guidelines for the Use of Data-Matching in Commonwealth Administration be elevated to mandatory legislative rules. The basis for this decision was that Commonwealth authorities were voluntarily complying and there was no evidence of non-compliance. In direct contradiction of this advice, the proposed measure would repeal the Guidelines as they apply to the ATO, and replace them with nothing.

## Penalties and remedies for non-compliance

The discussion paper contemplates applying the existing administrative penalty regime in Divisions 284 and 286. While this would be easy from Treasury's point of view, it would be inappropriate.

Consider the range of conduct that could be classified as non-compliance (or, in terms of the administrative penalties, "false statements"):

- a clerical error within the reporting entity results in incorrect information being reported to the ATO;
- a programing error within the reporting entity results in unreadable or incorrect information being reported to the ATO;
- the reporting entity's data is formatted differently to the ATO's specification, for example, address fields are split or merged;
- the reporting entity is reckless in compiling or transmitting its report, resulting in unreadable or incorrect information;
- the reporting entity refuses to report anything;
- the reporting entity deliberately provides false information.

These behaviours do not fit into the same spectrum of unreasonable-reckless-intentional false statements that apply to statements made by an entity in relation to its own affairs. Indeed, for several of these behaviours, the proper response would not be a penalty but a cooperative effort to fix the problem and ensure more useful data going forward.

While a taxpayer has a fundamental duty to maintain records to document their own tax affairs, and provide information to the ATO on the basis of that standard, no such principle exists for third parties.

The reality is that the proposed measure asks reporting entities to recycle data about other entities, which they hold in a form and to a standard that suits their specific needs, and give it to the ATO for the ATO to make whatever use of it they can. Where a reporting entity holds data about other entities, it implicitly accepts the risk that such information is incorrect or poorly-handled; this risk is entirely internal to that entity. The proposed measure goes too far if it forces reporting entities to collect, verify and process information about other entities to a standard which it simply does not need for its own purposes.

It is unlikely, despite the ATO's demand that all data be perfect and served according to the ATO's desires, that the ATO will actually tell reporting entities that a given report was OK or not. Administrative penalties can be applied at any time. Reporting entities should not be subject to fines, or have the risk of fines hanging over their heads indefinitely.

Third party reporting is not a core civic duty. It is an additional, recent impost created by a government that wants to extract tax by the most efficient, automated process possible. In that sense, it is unjustified for the Commonwealth to be too demanding of reporting entities.

It is important that a reporting regime be backed by sanctions for transgressions, otherwise the regime is impossible to enforce. The justification for the penalty lies in preventing the avoidance of the purposes of the regime. Therefore, penalties for reporting entities should be restricted to those cases where:

- the reporting entity intentionally make a false report, or
- the reporting entity was reckless and the non-compliance resulted in an actual prejudice to the revenue (such as actual tax avoidance going undetected).

For lesser non-compliance, it should be open to the ATO to apply to a Court for an injunction, requiring the reporting entity to report properly. While the injunction is in place, any non-compliance would be contempt of court. It is reasonable that non-compliance with a reporting obligation, after being formally warned, would result in penalties.

The requirement to go to a Court, instead of letting the ATO issue its own order, allows an independent judge to apply notions of fairness and reasonableness. This will be particularly important if the ATO attempts to apply the law too strictly, demanding precise encodings and high data standards.

To minimise the burden on the court system, the ATO should be empowered to enter into voluntary enforceable undertaking with reporting entities. The Commonwealth already has boilerplate code/legislation in the promoter penalties regime, AML/CTF Act, etc.

The third party reporting regime is predicated on collecting data from a relatively small number of important hubs in financial information flows, rather than from numerous taxpayers. Therefore it is not unreasonable for the ATO to have to, from time to time, provide assistance and a collaborative approach to making the reporting work. This is also consistent with the ATO's professed desire to collaborate, co-design, etc.

It is clear that penalties for technical breaches of the reporting regime are completely unacceptable.

## The ATO should, at least in practice, accept the data that the reporting entity has and not strictly enforce the power to specify a data format and medium

The discussion paper notes that the proposed measure would enable the ATO to specify "the precise form of information required". It is likely that the proposed measure will include legislation requiring reporting entities to provide the report in the ATO's desired format, otherwise the ATO will deem the reporting entity to have failed to lodge the report.

The ATO should not strictly enforce the power to specify the form of data.

The ATO should, at least in practice, accept the data in any format that is reasonably convenient for the reporting entity to produce, as long as:

- the data is machine-readable;
- the data is not too ambiguous for data-matching;
- the required data points (such as address, date of birth, etc) are present.

Even if, for example, the address fields are not split up the way the ATO would like, or the date of birth is not in the ATO's desired format, the ATO should accept this data. The ATO can use computers to parse the data provided to get the data it needs.

The fact that the ATO wants to be able to specify the data format, when it has been getting and using bulk non-legislative data without that ability for years, suggests that the ATO has been struggling with the various formats and contents of data sources. Perhaps it has data that it cannot write code to deal with, and accordingly has gaps in its coverage of data-matching, or has areas where data-matching is particularly inaccurate. Such a struggle, if it exists, is entirely due to the ATO's lack of capability.

Imposing a cost on reporting entities to output something to suit, down to the precise details, the ATO's desires, is unjustified. It is particularly unjustified where the "need" for a given format is artificially created by the ATO's own failures and mistakes.

The time required to create systems to extract information from various formats is not a legitimate argument for the data specification power. If it is time-consuming for the ATO, it would be time-consuming for the reporting entity too. The reporting entity should not have to bear a cost that the ATO can, and should, bear.

It is entirely feasible for a large, sophisticated entity such as the Commonwealth or the ATO to extract the information it needs from nearly any format of data that a reporting entity may have.

The ATO should only enforce the power to specify a data format/specification/medium etc in cases where the taxpayer has clearly and deliberately obfuscated the data by, for example,

- making up a proprietary format for no objectively-discernable purpose than to obstruct the ATO, or

- arbitrarily changing formats from one report to the next, for no objectively-discernable purpose than to obstruct the ATO.

In such an extreme case, consideration should be given to charging the reporting entity with the offence of obstructing a Commonwealth public official.

## The Commonwealth should bear any additional costs imposed on reporting entities

It is the Commonwealth that wants the data for a Commonwealth purpose. The Commonwealth should pay for it.

Consider that:

- the ATO routinely pays for non-legislative data, despite a lack of legislative obligation to do so;[1] and
- the ultimate alternative, in the face of non-compliance, is for the ATO to take physical access to premises and extract data at its own expense.[2]

A market-based approach to government requires that the burden of costs falls on the person who obtains the benefit.

A reporting entity should be entitled to present the ATO with a schedule of costs for setting up systems, gathering data, and extracting and formatting data, such as overtime, the cost of contractors and (particularly for small businesses) lost income from the diversion of key personnel to compliance tasks.

If the ATO does not want to pay the costs associated with third party data, then it can either:

- decide to go without, and exempt the entity form their reporting obligations, or
- take physical access to the reporting entity to obtain the required data at its own expense.[3]

If the Government decides not to require the ATO to pay reporting entities' costs, then it should require the ATO to collect, and publish in its annual report, information on the costs incurred by reporting entities. This will allow the people, and Parliament, to see the true cost of the regime.

[1] Inspector-General of Taxation, 'Review into the Australian Taxation Office's compliance approach to individual taxpayers – use of data matching' (2013) para 1.49.

[2] Using a power such as section 263 of the Income Tax Assessment Act 1936.

[3] This suggestion would make most people think, "No, you wouldn't take physical access except on a suspected tax evader, otherwise the imposition of physical access is unfair, since the business operator being interrupted has done nothing wrong." Bingo. The imposition of third-party reporting is inherently unfair.