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GST Administration Issues

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GST Administration Issues

1 OVERVIEW

The limited purpose of this paper is to discuss some selected aspects of GST administration relating to:

- GST rulings
- Refunds
- General Interest Charge (GIC)

It is appropriate to evaluate GST administration issues by reference to the well known hallmarks of a good tax system: equity, efficiency and simplicity.[1]

Equity, or fairness, has two dimensions: horizontal equity, which means that people in similar economic circumstances should be treated similarly; and vertical equity, which means that people in different situations should be treated differently, with those who are better off bearing a greater share of the tax burden.[2] A tax which places significantly different burdens on a taxpayer in similar economic circumstances is manifestly unfair.[3]

An efficient tax system is necessary in order to improve Australia's economic performance. With a more efficient tax system, resources will be more likely to move into activities where they will generate the largest economic gains to the nation, rather than activities where they will simply yield the largest tax gains to investors.[4] Any tax will tend to discourage the activity on which it is imposed; it follows that the more comprehensive the tax system is the less distortion there will be of the relative rewards of different types of work, of the relevant attractions of work and leisure, of the relative returns from different types of investment, and of the relative prices of goods and services.[5]

A good tax system should be as simple as possible. A complex tax system makes it difficult for people to understand the law and apply it to their circumstances. Complexity imposes high compliance costs on the community and high administrative costs on the tax authorities. Complex tax laws also result in socially unproductive and costly tax litigation.[6]

The criteria of equity, efficiency and simplicity are often contradictory. Greater efficiency can lead to reduced equity, and so on. A balancing act is therefore required which inevitably turns upon matters of judgement. The context within which that judgement is made can be important in attaching more or less weight to each criterion. An understanding of the nature of GST is essential in providing that context.

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[1] Reform of the Australian Tax System (Draft White Paper) (Canberra: AGPS, 1975), at paras 1.1 and 1.14.
[2] Id, at para 1.2.
[3] Id, at para 1.3.
[4] Id, at para 1.1.
[5] Id, at para 1.7.
[6] Id, at para 1.8.

'Broadly speaking, the GST is a tax on private consumption in Australia' which 'taxes the consumption of most goods, services and anything else in Australia, including things that are imported'.[7] The expression 'consumption' is not defined in the GST Act[8] and is not one of the 'basic rules' contained in Chapter 2 of that Act. The expression appears in several places in the GST Act but invariably for a specific purpose, such as defining the boundaries of GST-free food,[9] GST-free drugs and medicines,[10] and GST-free exports and other supplies for consumption outside Australia.[11]

The taxing of private consumption in Australia is generally achieved by:

- imposing tax on supplies made by entities registered for GST; but
- allowing those entities to offset the GST they are liable to pay on supplies they make against input tax credits for the GST that was included in the price they paid for their business inputs.[12]

In this way GST is effectively a tax on 'final' private consumption in Australia,[13] and is imposed on a registered supplier in respect of a supply made to a recipient.

It is a reality that most suppliers are unpaid tax collectors on whom the burden of the tax is not intended to fall, and that these suppliers must make judgements about the application of the tax to numerous transactions which occur on a day to day basis. Many suppliers would value certainty over most other factors. That is, many suppliers would prefer a taxable treatment that is certain to a non-taxable treatment that is not.

2 GST RULINGS

The Government has previously recognised that a rulings system, binding on the Commissioner, gives taxpayers a greater measure of certainty and fairness. In introducing the private binding rulings system, the Minister assisting the Treasurer said: 'The new system of binding and reviewable rulings will promote certainty for taxpayers and thereby reduce their risks and opportunity costs. The new system will also be fairer because taxpayers will be able to object to private rulings and have the matter reviewed by an independent tribunal or court.'[14] This cannot be said for the GST rulings system.

The only legislative reference to GST rulings is to be found in section 105-60 in Schedule 1 to the *Taxation Administration Act 1953* (Cth)('TAA').[15] There is a common

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7 Explanatory Memorandum to the A New Tax System (Goods and Services Tax) Bill 1998, Executive Summary, at 6.
8 *A New Tax System (Goods and Services Tax) Act 1999* (Cth) ('GST Act').
9 GST Act, subdivision 38A.
10 GST Act, section 38-50.
11 GST Act, subdivision 38E.
12 Explanatory Memorandum to the A New Tax System (Goods and Services Tax) Bill 1998, Executive Summary, at 6.
13 Ibid.
14 P Baldwin, Minister for Higher Education and Employment Services and Minister Assisting the Treasurer, Second Reading Speech, Taxation Laws Amendment (Self-Assessment) Bill 1992, 26 May 1992, Vol H of R 184 at 2774-2775.
15 Many provisions in the *Taxation Administration Act 1953* (Cth) were renumbered earlier this year, unnecessarily adding to the complexity of the taxation system by adding to the burden of compliance and administration. Taxpayers and their advisers had to familiarise themselves with renumbered provisions in an exercise akin to learning a new language. The Tax Office has had to do

misconception that this provision is the source of the power to issue rulings.[16] However, GST rulings are issued pursuant to the Commissioner's general power to administer indirect tax laws.[17] That distinction is of some importance if, for example, a taxpayer seeks to review, pursuant to the *Administrative Decisions (Judicial Review) Act 1977* (Cth) ('the ADJR Act'), the decision of the Commissioner to issue a particular ruling, since it is unlikely that a decision made pursuant to a general power of administration is one made under an enactment.[18] This stands in contrast to the Commissioner's view that a decision not to issue a ruling is reviewable under the provisions of that Act.[19] Nevertheless, the remedies available pursuant to section 39B of the *Judiciary Act 1903* (Cth) would still be available.

Section 105-60 applies to you if:

- the Commissioner alters a previous ruling that applied to you; and
- relying on the previous ruling, you have underpaid a net amount or an amount of indirect tax, or the Commissioner has overpaid an amount under section 35-5 of the GST Act, in respect of certain supplies and acquisitions that happened before the alteration.[20]

This provision draws heavily from the sales tax rulings system which preceded the GST, rather than from the income tax rulings system.[21]

A previous ruling must have 'applied to you' if you are to obtain the protection afforded by the statute. It is therefore important that the facts on which the ruling was based be clearly identified.[22] As with the income tax rulings system, a distinction might well be drawn between how the law applies to a particular set of facts, and 'the principles or reasoning' stated in the ruling.[23]

As Merkel J has commented: 'By making a ruling that states that it is binding 'to the extent it is capable of being a public ruling', or that a particular arrangement is 'likely to be regarded as a hire purchase arrangement', or that tax treatment of a particular arrangement is to be 'generally' as outlined the Commissioner is not providing the certainty that binding public rulings are intended to provide. Further, rulings in such terms obviously have a tendency to mislead which is antithetical to the system of certainty and fairness intended to be provided to taxpayers by the public rulings system.'[24]

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the same but must also change numerous publications to reflect the renumbering. There seems little accountability in imposing such a change on the tax community which comes with considerable cost and little or no benefit.

16 See, for example, Australian National Audit Office ('ANAO'), The Australian Taxation Office's Administration of Taxation Rulings (2001), which states, at para 1.6: 'GST private rulings are issued under s37 of the TAA'.

17 *Taxation Administration Act 1953 (Cth)*, Schedule 1, s356-5.

18 See *Hutchins v DFC of T* (1994) 94 ATC 4,443.

19 GSTR 1999/1, para 24.

20 *Taxation Administration Act 1953* (Cth), s105-60(1)(a) and (b).

21 Compare *Sales Tax Assessment Act 1992* (Cth), s77, and *Sales Tax Procedure Act 1934* (Cth), s 12D.

22 See *Bellinz Pty Limited v FC of T* (1998) 98 ATC 4399 at 4405; and (1998) 98 ATC 4634.

23 Id, at 4413 per Merkel J.

24 Id, at 4417 per Merkel J.

Note also that you must have 'relied' upon a GST ruling to obtain protection,[25] which is quite different to the income tax rulings system.

Unless the Commissioner is satisfied that you contributed to the giving, or continuing in force, of the earlier ruling by a misstatement or by suppressing a material fact, the underpaid indirect tax ceases to be payable, or the overpaid amount is taken to have been payable in full, from when the previous ruling was made.[26]

There are rules for deciding whether a ruling applies to you, or whether a ruling has been altered:

- a private ruling only applies to the entity to whom it was given;
- so far as a private ruling conflicts with an earlier public ruling, the private ruling prevails;
- so far as a public ruling conflicts with an earlier private ruling, the public ruling prevails;
- an alteration that a later ruling makes to an earlier ruling is disregarded so far as the alteration results from a change in the law that came into operation after the earlier ruling was given.[27]

There are likely to be numerous cases where a taxpayer with a private ruling will be unaware that a later public ruling has altered the previous ruling.

2.1 Public GST Rulings

Six years after the introduction of GST, the overall standard of public GST rulings continues to be high and demonstrate a high level of technical expertise and clarity.

In 2001 the Auditor-General found that the processes for the production of public rulings of high technical quality operated effectively overall.[28] He concluded that 'the mechanisms in place for public rulings substantially provide for consistent and fair treatment for taxpayers'.[29] One area of concern identified by the Auditor-General was the time taken to produce some types of public rulings, which inhibited their usefulness. He nevertheless concluded that 'the public rulings system, overall, provides taxpayers with increased certainty regarding the Commissioner's application of the tax law.'[30]

The time taken between draft and final rulings continues to be of concern. By way of example, GSTR 2003/D7 relating to s38-190(3) issued in draft on 19 December 2003, while GSTR 2005/6 issued in final on 14 December 2005.

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[25] See *Magna Stic Magnetic Signs Pty Ltd & Ors v FCT* (1989) ATC 5000.
[26] *Taxation Administration Act 1953* (Cth), s105-60(2).
[27] *Taxation Administration Act 1953* (Cth), s105-60(3).
[28] Australian National Audit Office ('ANAO'), The Australian Taxation Office's Administration of Taxation Rulings (2001), para 12. See also ANAO, Administration of Taxation Rulings Follow-up Audit (2004).
[29] Id, at para 17.
[30] Id, at para 26.

An extended period of uncertainty, and the unfair burden this places on the unpaid tax collector, hardly needs elaboration. I readily accept that some GST issues are very complex, and the interpretation of s38-190(3) certainly falls into that category. But that is exactly the problem for the unpaid tax collector self-assessing on a day to day basis. And it is precisely because an issue is complex that a measure of certainty is required. It is cold comfort for the taxpayer who gets it 'wrong' to be told that the Commissioner will take this into consideration in remitting penalties. The primary liability is often in practice irrecoverable from a consumer, and the unpaid tax collector suffers a very real loss.

Given the need for certainty by unpaid tax collectors with numerous day to day transactions, a taxpayer should be allowed to rely upon a draft ruling six months after its release if the final ruling has not issued by that date.

Private GST Rulings

There has been a great deal of scrutiny of the private rulings system.[31] The overall standard of private GST rulings is variable and often stands in marked contrast to public GST rulings, no doubt because of the vast number of private ruling requests received by the Commissioner. For this reason, the mechanism for reviewing a private GST ruling is of great importance, and yet there exist no formal review rights.

As discussed earlier in this paper, the Government has previously recognised that a rulings system, binding on the Commissioner, is fairer because taxpayers are able to object to private rulings and have the matter reviewed by an independent tribunal or court.[32] The Auditor-General in his 2001 report also recognised that a framework for rulings with formal review rights is a worthwhile feature of a rulings system supporting taxpayers in a self-assessment environment.[33]

However, no formal appeal rights exist in relation to private GST rulings. The issue of a private GST ruling does not give rise to objection and appeal rights, nor does it give rise to rights under the ADJR Act.[34] One means of challenging a private ruling is to invoke the assessment process by requesting a special assessment, and then proceed to objection and appeal.[35] Another means is to seek declaratory relief.

Declaratory proceedings were a common feature of sales tax disputes. For many years these proceedings were commenced in the state Supreme Courts or the High Court but not in the Federal Court. The first cases were replete with jurisdictional issues.[36] This prompted the Commissioner to issue Sales Tax Ruling ST 2454. This ruling dealt with sales tax objection and appeal procedures; jurisdiction and standing in declaratory

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[31] See Sherman, Report of an Internal Review of the Systems and Procedures relating to Private Binding Rulings and Advance Opinions in the Australian Tax Office, August 2000; and Australian National Audit Office ('ANAO'), The Australian Taxation Office's Administration of Taxation Rulings (2001).

[32] P Baldwin, Minister for Higher Education and Employment Services and Minister Assisting the Treasurer, Second Reading Speech, Taxation Laws Amendment (Self-Assessment) Bill 1992, 26 May 1992, Vol H of R 184 at 2774-2775.

[33] ANAO, 2001, at para 3.3.

[34] See *Hutchins v DFC of T* (1994) 94 ATC 4,443.

[35] See *Taxation Administration Act 1953* (Cth), ss 22-23.

[36] See *Kodak (Australasia) Pty Ltd v Commonwealth* (1989) 89 ATC 4010; *In Re the Totalisator Administration Board of Queensland* (1988) 88 ATC 4178; and *FC of T v Biga Nominees Pty Ltd* (1988) 88 ATC 4270.

proceedings; and disputing sales tax liability generally. The Commissioner indicated in the ruling that he would not continue with jurisdiction and standing challenges to declaratory proceedings. The original jurisdiction of the Federal Court was expanded in 1997 to include, among other things, any matter arising under any laws made by the Parliament, other than in respect of certain criminal matters.[37]

Six years after the introduction of GST it would be helpful for the Commissioner to issue a practice statement dealing with the issues likely to arise in the course of GST disputes.

One very real consequence of a lack of appeal rights is that it becomes very difficult to obtain certainty in relation to proposed transactions. You cannot enliven the objection and appeal process by requesting a special assessment as there is nothing to assess in relation to a proposed transaction. It would also be difficult to obtain a declaration in relation to a proposed transaction as it is not the role of the courts to provide advisory opinions.

The Inspector-General of Taxation has indicated that he intends to examine whether the current objection and appeal process provides timely resolution of disputes, citing the example where the Commissioner applies a ruling in an audit and all the facts are agreed.[38]

2.2 Improving the rulings system

In 2002 I made a number of recommendations to improve the GST rulings system.[39] These recommendations were adopted by the Law Council of Australia and discussed at the National Tax Liaison Group meeting on 5 December 2002. Several bear repeating, together with the ATO response at the time and what has happened since.

1. The Government should amend the GST law to provide formal review rights in respect of private GST rulings as a means of supporting taxpayers in a self-assessment environment, especially in relation to prospective transactions. The simplest path is to extend the private binding rulings regime to GST.

At the NTLG meeting in 2002, the ATO stated it 'would support a recommendation to Treasury to amend GST and related legislation to provide an appropriate legislative basis for GST Rulings and welcomes the opportunity to participate in proposing this as part of any NTLG process currently being developed.'

After almost four years we are yet to see any legislative change.

2. The Commissioner should issue a practice statement, along the lines of former Sales Tax Ruling ST 2454, dealing with GST objection and appeal procedures; jurisdiction and standing in declaratory proceedings; and disputing GST liability generally.

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[37] Judiciary Act 1903 (Cth), s 39B(1A).
[38] D Pengilley, *Highlighting the Tax Office's approach to Settling and Finalising Issues with Taxpayers*, 2nd Annual Corporate Tax Forum, 25 September 2006.
[39] K O'Rourke, *The GST Rulings System – Is it Failing?,* (2002) 12 Revenue LJ 79.

At the NTLG meeting in 2002, the ATO agreed 'that a practice statement along the lines suggested would provide some useful guidance for taxpayers. The preparation of such a statement, however, needs to be weighed against competing priorities.'

After almost four years we are yet to see any practice statement.

3. The Commissioner should withdraw and re-issue GSTR 1999/1, correcting the statement at paragraph 24 that a decision not to issue a ruling is reviewable under the provisions of the ADJR Act.

At the NTLG meeting in 2002, the ATO stated that it had 'undertaken a review of all formal public GST rulings for accuracy, consistency and currency - this recommendation will be included in that review.'

After almost four years we are yet to see the re-issue of GSTR 1999/1.

To these recommendations I would add the following.

4. The Commissioner should issue a public ruling allowing a taxpayer to rely upon a draft ruling six months after its release if the final ruling has not issued by that date.

3 REFUNDS

If the net amount for a tax period is less than zero, the Commissioner must, on behalf of the Commonwealth, pay that amount to you.[40] The entitlement to the refund arises when you give the Commissioner a GST return.[41] However, there are restrictions and time limits on claiming refunds.

3.1 Restrictions on claiming refunds

Section 105-65(2) of Schedule 1 to the *Taxation Administration Act 1953* (Cth), headed 'Restriction on refunds', applies to so much of any amount of indirect tax as you have overpaid, and to so much of any net amount that is payable to you under section 35-5 of the GST Act as the Commissioner has not paid to you or applied under Division 3 of Part IIB of the *Taxation Administration Act 1953* (Cth).

If you overpaid an amount, or the amount was not refunded to you, because a supply was treated as a taxable supply to any extent, and the supply is not a taxable supply to that extent (for example, because it is GST-free), then the Commissioner need not give you the refund, or apply the amount under Division 3 or 3A of Part IIB, if the Commissioner is not satisfied that you have reimbursed a corresponding amount to the recipient of the supply, or if the recipient is registered or required to be registered.[42]

Where the Commissioner is not satisfied that the relevant conditions are met, then he 'need not give you the refund'. Whether he still has a discretionary power to refund

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[40] GST Act, s35-5.
[41] GST Act, s35-10.
[42] *Taxation Administration Act 1953* (Cth), s105-65(1).

remains an open question.[43] The Commissioner's current practice is governed by Practice Statement PS LA 2002/12.

If the supplier has reimbursed the recipient, a refund will be allowed. In the case of an unregistered recipient, the ATO must refund the amount pursuant to section 8AAZLF of the *Taxation Administration Act 1953* (Cth). In the case of a registered recipient, The ATO will exercise the section 105-65 discretion to allow the entitlement or refund.

If the supplier has not first reimbursed the recipient, the ATO will generally not exercise the section 105-65 power to allow a refund.[44]

In the case of an unregistered recipient, there are two stated exceptions to this but it is now doubtful whether they have current application.[45] The first exception applies if the supplier can demonstrate that it has absorbed the cost of the amount incorrectly included as GST in the price and did not pass it on to the consumer. Before allowing such a refund, the ATO would require from the supplier conclusive and tangible proof of its claims. However, there was an expectation that such instances would be limited to supplies that were made very soon after the GST was implemented on 1 July 2000. The second exception applies if the supplier had complied with a written directive from the ACCC in relation to supplies that occurred before 30 June 2002 (for example, where the recipients could not be readily traced, such as for numerous supplies made to cash customers in the public at large).

In the case of a registered recipient, there are also two stated exceptions.[46] The first exception applies if the supplier can demonstrate that it has absorbed the cost of the amount incorrectly included as GST in the price, did not pass it on, and has cancelled earlier tax invoices sent to the registered recipients. The ATO will require tangible proof of such claims. The second exception applies in cases where genuine financial hardship may result from any refusal to refund the amount incorrectly included as GST in the price. An example would be where the supplier had not received payment from the recipient. However, before making any refund to the supplier, the ATO will require that earlier tax invoices have been cancelled.

3.2 Reimbursement

Section 105-65 refers to you having 'reimbursed a corresponding amount to the recipient of the supply.' That is, where the burden of the tax has been passed on to a recipient, reimbursement of the recipient is generally required before a refund will be made. The recent decision of the High Court in *Avon Products*[47] on the meaning of 'passing on' under the sales tax law has direct relevance to the meaning of 'reimbursement' under the GST law.

The High Court noted that a 'central feature' of sales tax was that 'the economic burden of the impost is generally not intended to be borne by the person liable to remit it; it is to

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[43] See generally *Finance Facilities Pty Ltd v FCT* (1971) 127 CLR 106; [1971] HCA 12.
[44] PS2002/12, para 5.
[45] PS2002/12, Appendix 2.
[46] PS2002/12, Appendix 2.
[47] *Avon Products Pty Limited v Commissioner of Taxation* [2006] HCA 29.

be passed on.'[48] This statement is true for indirect taxes generally and is what distinguishes them from direct taxes, such as income tax.

The High Court noted that 'there is nothing extraordinary in the proposition that in the usual course of things sales tax will be passed on.'[49] There is then a curious statement that, 'leaving aside rare cases where sales tax is separately identified and superadded to the invoice price after sale, sales tax can only be passed on indirectly through the price mechanism.' Far from being rare, it was a requirement that sales tax be separately identified at the most frequently occurring taxing point, which was the last wholesale sale. Avon involved a less frequent taxing point, an 'indirect marketing sale',[50] which imposed tax on the retail sale at a notional wholesale selling price.[51] There was no requirement here to separately identify the sales tax on the invoice.

The relevant provision in Avon applied in cases of 'Tax Overpaid', where the 'claimant has paid an amount as tax that was not legally payable.' The amount of the credit was 'the amount overpaid, to the extent that the claimant has not passed it on.'[52] The legislation did not provide a comprehensive definition of 'passed on', which therefore had to be determined according to its ordinary meaning.[53]

A number of propositions emerge from the decision of the Court:

1. The onus of proving that the taxpayer has not passed on the overpayment lies upon the taxpayer.[54] This will occur comparatively seldom.[55]

2. The question whether sales tax has been passed on is a question of fact.[56]

3. Where the facts disclose that the taxpayer has set prices at a level to ensure that they exceed cost (including tax), it will be difficult for the taxpayer to satisfy its onus of proof that it has borne the tax burden itself.[57]

4. The contention that a tax is only passed on if the price at which the goods are sold is increased by the amount of the tax is flawed.[58]

In my opinion, these propositions are equally applicable to reimbursement under GST.

In the light of *Avon*, and given the apparent redundancy of some of the material in Practice Statement PS LA 2002/12, it would be highly desirable for the Commissioner to update and re-issue that Practice Statement.

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[48] [2006] HCA 29 at [7].
[49] [2006] HCA 29 at [9].
[50] *Sales Tax Assessment Act 1992* (Cth), s20.
[51] *Sales Tax Assessment Act 1992* (Cth), s16, Schedule 1, Table 1, Assessable Dealings AD2d and AD12d.
[52] *Sales Tax Assessment Act 1992* (Cth), s51(1), Schedule 1, Table 3, Credit Ground CR1.
[53] [2006] HCA 29 at [6].
[54] Id at [5]; see also *Taxation Administration Act 1953* (Cth), s14ZZO(b).
[55] Id at [12].
[56] Id at [20].
[57] Id at [21].
[58] Id at [23].

3.3 Wash transactions

The ATO recognises that reversing transactions and revising every activity statement to correct errors between registered entities amounts to a paper 'round robin' among the registered recipient, the supplier, and the ATO. Significant compliance costs are incurred with no change to the financial result. Accordingly, the ATO has accepted an alternative solution that results in no detriment to GST revenue.[59]

When input tax credits are claimed in good faith before it is discovered that non-taxable supplies were treated as taxable, the ATO will adopt the alternative solution, but only where both the supplier and the recipient meet specified conditions.[60] Further, neither party is obliged to adopt the solution, even if they both meet the criteria.

The General Interest Charge (GIC) that would otherwise be payable by the recipient is effectively waived under this solution.[61]

The alternative solution cannot be extended to any circumstances outside of those covered by section 105-65 of the *Taxation Administration Act 1953* (Cth). For example, the solution cannot be applied to the reverse scenario of the incorrect treatment of a taxable supply as non-taxable. Such errors must be corrected either by activity statement revision or using Fact Sheet NAT 4700 (Correcting GST Mistakes).[62]

3.4 Time limit on claiming refunds[63]

You are not entitled to a refund under section 35-5 in respect of a particular tax period or an input tax credit that is attributable to a particular tax period, unless you notify the Commissioner that you are entitled to the refund or credit within four years after the end of the tax period.[64]

The Explanatory Memorandum which introduced the materially identical predecessor to section 105-55 was tolerably clear in stating that 'entitlements to refunds, input tax credits and diesel fuel credits will expire 4 years after the end of the tax period to which they relate.'[65]

But section 105-55 imposes no time limit on the claiming of a refund if there is a positive net amount for the tax period in which the overpayment occurred. This is because section 105-55 requires you to identify the particular tax period to which the refund under section 35-5 of the GST Act relates. Section 35-5 in turn provides for a refund if 'the net amount for a tax period is less than zero'. If there is a positive net amount for the tax period in which the overpayment occurred, section 105-55 has no application as there is neither a refund under section 35-5 of the GST Act nor any input tax credit foregone. An ATO Fact Sheet confirms this, stating that 'if you do not claim your refund or notify us of

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[59] PS2002/12, para 17.
[60] PS2002/12, paras 22-23.
[61] PS2002/12, para 20.
[62] PS2002/12, para 21.
[63] See generally P Stacey, *Raising the 4-year Bar on Reclaims*, (2004) 4 AJGST 191; M Bennett, *GST time limits – under or over the net*, (2005) 5 AGSTJ 69.
[64] *Taxation Administration Act 1953* (Cth), Schedule 1, s105-55.
[65] A New Tax System (Goods and Services Tax Administration) Bill 1998, at para 3.28.

your entitlement within the four year limit, the maximum refund you can claim will be limited to an amount equal to what you paid the Commissioner for the relevant tax period.'[66]

The Fact Sheet gives, as Example 2, 'Mike's Mowing paid a tax liability of $3,000 for his January 2001 activity statement. Mike has recently reviewed this activity statement and realised he has an outstanding GST refund of $500. The four year time limit does not apply as the GST refund claim for $500 is less than the $3,000 he originally paid to the Commissioner.'

The Fact Sheet gives, as Example 3, 'Fred's Fruit paid a $3,000 tax liability for his July 2000 return. Fred checked his July 2000 activity statement and realised he had made a mistake. He should have received $1,000 back instead of paying $3,000. If he claims the GST refund by 31 July 2004, Fred's Fruit is entitled to receive the $4,000 difference. After this date, the four year time limit takes effect and Fred is only entitled to receive a GST refund of the $3,000 which he paid.'

Similarly, if an input tax credit is mistakenly excluded from a GST return, the interaction of section 105-55 of the TAA and section 29-10 of the GST Act operate to defer the four year rule indefinitely. As above, section 105-55 of the TAA requires you to identify the particular tax period to which the refund under section 35-5 of the GST Act relates, and section 35-5 of the GST Act in turn provides for a refund if 'the net amount for a tax period is less than zero'. This will usually relate to a period in which an input tax credit is payable such that the four year rule commences at the end of the period. However, section 29-10(3)(b) of the GST Act can defer attribution of an input tax credit if a tax invoice is not held at the time the GST return is lodged. The input tax credit will instead be attributable to the first tax period for which you give the Commissioner a GST return that does take it into account.[67]

The ATO Fact Sheet confirms this. Under the heading 'When the four year limit may not apply', it states that 'if you have a valid tax invoice and have not claimed the GST credit for that purchase, you may claim the GST credit in the current or any later tax period, rather than revise a previous activity statement.'

The Fact Sheet gives as Example 1, 'Bob from Bob's Butcher found a tax invoice in his files dated 20 July 2000. The invoice entitled Bob to claim a GST credit. The four year time limit does not apply in this case because Bob has not made a claim using this invoice before, although four years has passed since the invoice date. Bob correctly claimed the full GST credit in his current activity statement.'

There are sound public policy reasons for limitation periods which go to the finality of disputes or potential disputes, and to certainty of financial position. In the case of the Commonwealth, it is entirely reasonable that the books be ruled off after four years in the certain knowledge that no further refunds will be due. This policy intent, clear in the Explanatory Memorandum, has miscarried in the drafting of section 105-55 of the TAA. It is also inequitable that some taxpayers are limited to a four year refund period while others enjoy an unlimited refund period based around arbitrary criteria, such as whether they happened to have a positive net amount in the relevant tax period. Section 105-55

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[66] www.ato.gov.au/businesses/content.asp?doc=/content/47026.htm, viewed 1 October 2006.
[67] GST Act, s29-10(4).

should be amended to provide a four year time limit on claiming refunds in all circumstances.

4 GENERAL INTEREST CHARGE

Liability to the General Interest Charge (GIC) is dealt with by section 162-100 of the GST Act. The GIC is automatically imposed and worked out in accordance with section 8AAC of the TAA, and the general discretionary power to remit is in section 8AAG of the TAA.

The GIC provides a case study in conceptual confusion between culpability and compensation. Conceptually, the penalty regime ought to be directed towards culpability while the GIC regime ought to be directed towards compensating the revenue for the time value of money. This distinction is well articulated in the ROSA report: 'An interest charge is ill suited to such a *de facto* penalty role, imposing an uncertain effect that depends significantly on factors other than the size of the shortfall and the degree of culpability. In particular, the effect of imposing a penalty interest on shortfalls would depend on the period taken for the shortfall to be identified and the rate at which the taxpayer would voluntarily have borrowed a similar amount. Furthermore, the perception that taxpayers are being penalised twice for the same offence, or being penalised where it was decided that no culpability penalty should apply, is undesirable.'[68]

The ATO has articulated the rationale for the GIC to be:

- to act as an incentive for payment of liabilities by their due date;
- to ensure that taxpayers who fail to fulfil their payment and return or statement obligations do not receive an advantage over those who meet their tax liabilities in full by the due date; and
- to compensate the community for the impact of late payments.[69]

In practice, however, there arise numerous examples where the GIC operates as a de facto penalty regime. The recent Practice Statement dealing with the remission of GIC, among other things, reinforces this view by seeking to make the taxpayer's compliance history a relevant consideration in certain circumstances.[70]

4.1 Brief history of the GIC [71]

In 1992, the interest and penalty elements of the penalty for underpaid tax were imposed under separate legislative provisions for the first time. The Explanatory Memorandum

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[68] Report on Aspects of Income Tax Self Assessment (ROSA), 16 December 2004, at 52; see also Inspector-General of Taxation, Review into the Tax Office's Administration of Penalties and Interest Arising from Active Compliance Activities, 18 May 2005, at para 3.16.

[69] PS LA 2006/8, at para 1.

[70] PS LA 2006/8, at paras 84 and 120.

[71] A useful summary of the history of GIC can be found in the report of the Inspector-General of Taxation, Review of the Remission of the General Interest Charge for Groups of Taxpayers in Dispute with the Tax Office, 5 August 2004, para 1.60ff.

which introduced the interest component described it as being 'compensation to the Revenue for the time value of money'.[72] The rate of interest was set at the 13 week Treasury note yield plus four percentage points.

In the Second Reading Speech to the Bill, the Minister assisting the Treasurer described the extra four per cent as reflecting administration costs and the fact that most taxpayers would not be able to borrow at the 13 week Treasury note rate. He also stated that the rate set for the new separate interest charge would make most taxpayers indifferent to borrowing from a bank or being liable to the interest at that rate. From the outset, therefore, the rate was set at four percentage points higher than was necessary to compensate the revenue for its loss. Nevertheless, the increase could be justified on maintaining equity between taxpayers by ensuring taxpayers didn't use the base interest rate as an alternative and cheaper source of finance.

The GIC regime in its current form was introduced on 1 July 1999 creating a single rate of interest payable where the correct payment was not received by the due date. From this date, the rate of pre-amended assessment interest was increased by a further four per cent. No explanation was given for this further increase in the Explanatory Memorandum to the Bill that introduced the uplift. According to the Inspector-General of Taxation, 'there is evidence from other material which suggests that this uplift was made to discourage taxpayers from using the tax system as an unsecured mechanism for borrowing. Another view is that this increase was part of a broad simplification package for interest generally.'[73] Neither reason is compelling. At this point the GIC became a de facto penalty regime in addition to compensating the revenue for its loss.

4.2 Wash transactions

According to the Commissioner, 'a GST 'wash' transaction is an expression used to describe the situation where a GST-registered supplier wrongly treats a taxable GST supply as non-taxable, hence underpaying its GST. However, the supply in question is made to a recipient who is registered for GST and would have been entitled to claim back from the Tax Office a full input tax credit if the transaction had been correctly treated as taxable by the supplier. The term 'wash' refers to the fact that the effect on primary GST revenue is neutral.'[74]

The GST is designed to have a self-policing element and an audit trail. It should be understood that this was a deliberate policy choice. This is why the ATO does not take kindly to arguments that, in business to business transactions, it is a 'wash' for GST with a liability and an offsetting credit. If business to business transactions were meant to be ignored, we could have had a retail sales tax or an 'additive' GST. But we do not, so business to business transactions matter.

Nevertheless, if the effect on primary GST revenue is neutral there is little need to compensate the revenue for the time value of money. The imposition of any GIC in

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[72] Explanatory Memorandum accompanying the Taxation Laws Amendment (Self Assessment) Bill 1992, Chapter 8.
[73] Inspector-General of Taxation, Review of the Remission of the General Interest Charge for Groups of Taxpayers in Dispute with the Tax Office, 5 August 2004, para 1.64.
[74] PS LA 2006/8 at para 119.

these circumstances is penal in nature. Remission in full is therefore in principle generally warranted. To do otherwise is inequitable.

Earlier in this paper we discussed those wash transactions covered by section 105-65 of the *Taxation Administration Act 1953* (Cth), and how the GIC is effectively waived in those circumstances.

The remission of GIC in all other wash transactions is governed by an earlier Practice Statement, PS LA 2003/2, in which the GIC will only be remitted to the base rate. Even then, other factors are taken into account, such as the taxpayer's compliance history. These other factors could only ever be relevant to culpability and seem misplaced.

It is therefore recommended that the Commissioner adopt the practice of remitting GIC in full on wash transactions unless there are special circumstances to do otherwise.

4.3 Pre-amended assessment interest

A distinction can be drawn between pre-amended assessment interest and post-amended assessment interest. As noted by the Inspector-General of Taxation, 'in the pre-amended assessment period a taxpayer may not be aware that there is an underpayment of tax. In fact, a taxpayer may genuinely believe that they have complied with all their taxation obligations under the self assessment regime. In such a situation it is unclear how the imposition of the interest charge in full without remission can serve to discourage the taxpayer from using the tax system as an unsecured mechanism for borrowing. Rather, it would be assumed that such a compliance effect would be more relevant in circumstances where a taxpayer has intentionally not complied with their taxation obligations or has delayed in the payment of tax.'[75]

The Inspector-General went on to say that, 'in this context, the imposition of the interest charge in full without remission during the pre-amended assessment period can have a punitive-like effect even though the taxpayer's circumstances do not warrant such an outcome.'[76]

This issue has been dealt with specifically in the income tax context by the introduction of a Shortfall Interest Charge (SIC) for amendments to the year of income ended 30 June 2005 and later years. It is a specific acknowledgement that taxpayers who are genuinely unaware of the shortfall may be unable to take any steps to reduce their exposure to GIC. The SIC is at a lower rate than the GIC and its purpose is to neutralise any advantage over others who pay the tax properly owing at the appropriate time.[77]

The Practice Statement makes no effort to acknowledge these circumstances in the context of GST, stating bluntly: 'As the SIC regime only applies to income tax shortfalls the above considerations do not apply to GIC imposed in respect of other shortfall amounts.'[78]

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[75] Inspector-General of Taxation, Review of the Remission of the General Interest Charge for Groups of Taxpayers in Dispute with the Tax Office, 5 August 2004, para 2.28
[76] Id at para 2.29.
[77] PS LA 2006/8 at paras 27-29.
[78] Id at para 44.

And yet, there seems no reason in principle why a SIC directed towards the pre-amended assessment period in an income tax context should be any less desirable in the GST context. It is inequitable to treat taxpayers differently, albeit in different taxation regimes, when their circumstances are in principle identical. It is also nonsensical for taxpayers to have a Running Balance Account, a single liability across all federal taxes, which in like circumstances calculates SIC on one part of the balance and GIC on another.

It is understood that Treasury is reviewing the possible extension of the SIC regime to all federal taxes. It is recommended that legislative change be effected as soon as possible to extend the SIC regime to GST shortfalls in the pre-amended assessment period.

Reliance on draft public rulings

As stated above, in the context of ruling protection for underpaid tax, the Commissioner should issue a public ruling allowing a taxpayer to rely upon a draft ruling six months after its release if the final ruling has not issued by that date. At the very least it should be expected that reliance on a draft public ruling, being the considered views of the Commissioner, should warrant GIC remission to the base rate, which would still compensate the revenue for the time value of money.

ROSA recommended that 'where taxpayers rely on public rulings while they are in draft form they should be protected from penalties and receive full remission of any interest charges in the event that the final ruling is issued in different terms, to their detriment.'[79] It is a curious recommendation as taxpayers who rely upon a draft ruling generally do so at their peril.

This peril is reflected in the recent Practice Statement which states that a 'draft public ruling will only be accepted by the Tax Office as representing general administrative practice [and thus warranting full remission of the GIC] where the view contained therein is supported by other evidence of a long term and consistent pattern of active Tax Office treatment of the issue consistent with the view expressed in the precedential material.'[80] This is a vague statement of uncertain application in practice. It would have been better to simply state that reliance on a draft public ruling would generally warrant remission of GIC to the base rate.

4.4 Appealing the GIC

The Inspector-General of Taxation has correctly noted, in the context of GST, that, 'currently, taxpayers who are seeking a review of the level of interest charged by the ATO can only do so by making an application for judicial review in accordance with the

[79] ROSA, Recommendation 2.7.
[80] PS2006/8 at para 105.

terms of the *Administrative Decisions (Judicial Review) Act 1977*. This is a costly and lengthy process.'[81]

In the context of income tax, the ROSA Report recommended that 'where unremitted shortfall interest exceeds 20% of the tax shortfall, the taxpayer should be entitled to object to the decision not to remit. Objection decisions should be subject to review and appeal where the shortfall interest remaining after determination of the objection exceeds 20% of the tax shortfall.'[82]

The ROSA Report went on to recommend that Treasury 'review the possible application of the recommendations contained in this report to all federal taxes.'[83] Significantly, the income tax amending legislation 'has been drafted so that it can be used as a generic model for application to other taxes if required. A further review exploring this possibility will be undertaken starting from the middle of this year [2005].'[84]

The outcome of the Treasury review is unknown but there seems no reason in principle why objection and appeal rights against the remission of interest imposed in the income tax context should be any less desirable in the GST context. It is recommended that legislative change be effected as soon as possible to extend objection and appeal rights to decisions to remit GIC on GST shortfalls where the interest amount exceeds 20% of the shortfall.

5 CONCLUDING REMARKS AND SUMMARY OF RECOMMENDATIONS

The administration of GST is by no means broken and is generally of a high standard. It is readily apparent, however, that improvements can and should be made, and that a sense of urgency needs to be injected into the process. Nine suggested recommendations are summarised below.

The limited purpose of this paper was to discuss some selected aspects of GST administration relating to GST rulings, refunds and the GIC. But three common themes emerged from even this limited discussion.

First, the lack of objection and appeal rights in both the private rulings regime and the remission of GIC on GST shortfalls. Second, the absence of Practice Statements in important areas of administration, or existing Practice Statements which are outdated and require revision in some material respects. Third, the lack of legislative consistency in income tax and GST administration. In each of these areas the unpaid tax collector deserves better.

The nine recommendations are:

1. The Government should amend the GST law to provide formal review rights in respect of private GST rulings as a means of supporting taxpayers in a self-assessment

[81] Inspector-General of Taxation, Review of the Remission of the General Interest Charge for Groups of Taxpayers in Dispute with the Tax Office, 5 August 2004, para 2.114.
[82] ROSA, at 57.
[83] ROSA, Recommendation 7.2.
[84] The Treasury, Consultation Letter on Exposure Draft of Second Tranche of Amendments arising from the Review of Self Assessment, May 2005.

environment, especially in relation to prospective transactions. The simplest path is to extend the private binding rulings regime to GST.

2. The Commissioner should issue a practice statement, along the lines of former Sales Tax Ruling ST 2454, dealing with GST objection and appeal procedures; jurisdiction and standing in declaratory proceedings; and disputing GST liability generally.

3. The Commissioner should withdraw and re-issue GSTR 1999/1, correcting the statement at paragraph 24 that a decision not to issue a ruling is reviewable under the provisions of the ADJR Act.

4. The Commissioner should issue a public ruling allowing a taxpayer to rely upon a draft ruling six months after its release if the final ruling has not issued by that date.

5. The Commissioner should update and re-issue Practice Statement PS LA 2002/12 in the light of *Avon*, and to remove some now redundant material.

6. The government should amend section 105-55 to provide a four year time limit on claiming refunds in all circumstances so as to maintain equity between taxpayers and provide finality and certainty in the Commonwealth's financial position.

7. The Commissioner should revise the recent Practice Statement dealing with the remission of GIC to make clear the distinction between culpability and compensation. In particular, the Commissioner should adopt the practice of remitting GIC in full on wash transactions unless there are special circumstances to do otherwise, and should remit GIC to the base rate for reliance on a draft public ruling which changes in the final ruling to the detriment of the taxpayer.

8. The Government should amend the TAA to extend the SIC regime to GST shortfalls in the pre-amended assessment period.

9. The Government should amend the TAA to extend objection and appeal rights to decisions to remit GIC on GST shortfalls where the interest amount exceeds 20% of the shortfall.

