

22 June 2018

By email: garnishee@igt.gov.au

Simon Ly
Senior Tax Complaints and Review Officer
Office of Inspector-General of Taxation
50 Bridge Street
Sydney NSW 2000

Dear Mr Ly

Review into the Australian Taxation Office's use of Garnishee Notices

The Consumer Action Law Centre (**Consumer Action**) welcomes the opportunity to comment on the Australian Taxation Office's (**ATO**) use of garnishee notices.

We reject the legal status quo which enables garnishee orders issued prior to bankruptcy to continue to garnish the wages of bankrupted individuals post-bankruptcy. As we understand it, garnishee orders issued by the ATO are considered to be a statutory charge, and therefore will continue to operate post-bankruptcy if issued prior to bankruptcy.¹ We have read and considered the common law basis for this legal position as articulated in the *Commissioner of Taxation v Donnelly*² and *Macquarie Health Corporation Ltd v FCT*³.

We also reject the legal status quo that permits the ATO to issue garnishee orders in exercise of its administrative powers, absent a court hearing, pursuant to subsection 260-5(2) of Schedule 1 to the Taxation Administration Act 1953 (Cth) (**TAA**).

We further reject the inflated limit for ATO garnishee orders which is 30% of income, compared with 20% for the private sector.⁴

Our comments are detailed more fully below.

¹ Australian Financial Security Authority, *Currently Bankrupt Garnished Wages and Frozen Bank accounts*, <https://www.afsa.gov.au/insolvency/i-am-currently-bankrupt/garnished-wages-frozen-bank-accounts>.

² *Commissioner of Taxation v Donnelly* (1989) 25 FCR 432.

³ *Macquarie Health Corporation Ltd v FCT* (1999) 96 FCR 238.

⁴ Australian Tax Office, PS LA 2011/18, Annexure C Statutory Garnishees, <http://law.ato.gov.au/atolaw/view.htm?Docid=PSR/PS201118/NAT/ATO/00001#P108>.



About Consumer Action

Consumer Action is an independent, not-for profit consumer organisation with deep expertise in consumer and consumer credit laws, policy and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling, legal advice, legal representation, policy work and campaigns. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just market place for all Australians.

Conflicting legislation

Bankruptcy brings with it a number of restrictions on an individual's lifestyle, including restrictions on income. A proportion of a bankrupt's income that is assessed as being in excess of the Australian Financial Security Authority's (AFSA) 'indexed amounts' is paid to the Official Trustee pursuant to a payment schedule.⁵ According to the AFSA's Official Trustee's practice statement, a bankrupted individual who earns over the threshold can "afford" to make contributions to paying down their debt, while still meeting all their necessary living expenses.⁶ It can therefore be assumed that AFSA has assessed that the indexed amounts are enough for bankrupted individuals and their families to live off, and were carefully calculated to permit an adequate standard of living.

The prerogative of allowing bankrupted individuals and their families to receive a basic income free from contributions to the Official Trustee is directly compromised by the ATO's use of garnishee orders that survive bankruptcy and continue to garnish income from indebted persons. It is conceivable that a bankrupted individual might earn less than the indexed amount, and therefore should be free from making income contributions, but will still be required to make payments under an ATO garnishee order. Such individuals and their families will therefore be forced to survive on an income that is below the carefully calculated 'indexed threshold' set out by AFSA and will not have access to income required to meet their basic living expenses as anticipated by AFSA.

Put simply, while the Official Trustee deems these low income bankrupted individuals too poor to make income contributions, the ATO considers that they are sufficiently wealthy to make payments under a garnishee order.

A possible counter-argument to this analysis is that a bankrupted tax debtor who is subject to a garnishee order will still be entitled to earn above an amount specified in his/her State's 'weekly compensation amount'. The 'weekly compensation amount' provides for a minimum 'net weekly amount of any wage or salary' that the judgment debtor requires to live off, and therefore cannot be garnished.⁷ For example, effective 1 April 2018, the 'weekly compensation amount' for NSW is \$500.60.⁸ However, this does not take into account the fact that bankruptcy brings with it a host of other restrictions on an individual's lifestyle, and the fact that the

⁵ Australian Financial Security Authority, Insolvency Indexed Amounts, <https://www.afsa.gov.au/insolvency/how-we-can-help/indexed-amounts-0>.

⁶ Australian Financial Security Authority, Official Trustee Practice Statement 1 Income Contributions, <https://www.afsa.gov.au/sites/g/files/net1601/f/otps1.pdf>.

⁷ NSW District Court, Garnishee Amounts, http://www.districtcourt.justice.nsw.gov.au/Pages/practice_procedure/garnishee_amounts.aspx.

⁸ Ibid.



'indexed amounts' outlined by AFSA best represents the amount of income required to cope financially in bankruptcy.

In addition, it is possible that an individual who earns more than the 'indexed threshold' might experience a reduction in income from two simultaneous sources, being their mandated income contribution to the Official Trustee as well as their garnished income to the ATO.

The impact of Garnishee Orders that survive bankruptcy

Consumer Action's National Debt Helpline regularly receives distressed calls from indebted individuals, many of whom have received garnishee orders which continue to garnish their wages post-bankruptcy. It is extremely difficult for these individuals to support themselves and their families on garnished wages, and they are often left unable to afford their existing accommodation, motor vehicle and modest lifestyle expenses. This stress is inflated further when they encounter unexpected financial obstacles, such as deteriorating health or relationship breakdowns.

Unlike other bankrupted individuals who become bankrupt as a result of private sector debt, there is no respite for the ATO debtor, as wages can be garnished regardless of the indexed threshold. This relentless garnishment of wages can lead to circumstances where the bankrupted individual no longer wishes to work, or is unable to work due to mental health issues.

In much the same way as other over-indebted individuals accumulate debt to private sector creditors, failure to comply with tax obligations is often described as coinciding with breakdowns in personal relationships, breakdowns in physical/mental health, or other shocks such as deaths in the family or failure of a small business. A failure to file tax returns and meet relevant ATO deadlines can be warning indicators of these external lifestyle stressors, as individuals are more focused on the immediate threats to their wellbeing than distant tax obligations.

As described by Foohey et al:

struggling with unmanageable debts can strain marriages and relationships. Fights over how to make ends meet, shifting of responsibilities for dealing with ever-worsening finances, and watching loved ones deal with the emotional distress that comes with money troubles may lead to separation and divorce. Splitting one household into two only worsens the financial problems.⁹

In contrast, the fresh start that bankruptcy should provide may actually salvage some relationships.¹⁰ However, despite their personal struggles, individuals with a tax garnishee will not receive the 'fresh start' that is afforded to other debtors who declare bankruptcy, and their financial struggles and stress triggers will continue unmitigated.

In the absence of free legal and financial advice from organisations like Consumer Action, bankrupted individuals with garnishee orders are more than likely unable to afford the private legal or accountancy advice needed to challenge—or for that matter even understand—the technical basis of the garnishee order. This

⁹ Pamela Foohey, Robert M. Lawless, Katherine Porter & Deborah Thorne, *Life in the Sweatbox*, Notre Dame Law Review, forthcoming 2018, p. 39.

¹⁰ *Ibid*, p. 40.



sense of frustration is compounded by the administrative nature by which ATO Garnishee orders are issued, and the denial of the debtor's 'day in court'.

Case Study: Dave's story

Dave (not his real name), a self-employed owner of a small business, spoke with the National Debt Helpline and explained that he was recently forced into bankruptcy due to a business debt he was unable to repay due to illness and reduction in work hours. In addition to the business debt, Dave had an ATO tax debt in excess of \$300,000. Dave told us that he has experience dealing with and honouring debts outstanding to the ATO. However, according to Dave, this latest \$300,000 debt notice (received before his bankruptcy), which was accompanied by a garnishee notice, came 'out of nowhere'. Dave explained that he remains extremely confused about the basis for this Garnishee order but, because of the immediate reduction of his income through the Garnishee order, he has not been able to afford the professional legal or accountancy advice that he desperately needs to understand or potentially challenge the order.

Dave expressed immense frustration with his financial situation in bankruptcy, explaining that, unless he earns less than \$800 a fortnight, the ATO takes out 40% of this income pursuant to the garnishee order. He emphasised how it was virtually impossible to support a family of three kids under these conditions. Dave also mentioned that he had recently suffered a stroke, which adds \$400-\$500 a month for medication expenses.

Dave felt that he was being treated as though he was a sophisticated company with support to manage its debts and tax obligations, when in reality he was just a self-employed small business owner. He noted that he was advised by the ATO get a "corporate administrator" but stated that the fees of corporate administrators were well beyond his budget.

Finally, Dave expressed his frustration in being effectively 'left out of the loop' of the process of servicing his own debt, as he has not received any updates on the amount owing, or how much longer it will take to reduce. Fortunately, Dave has recently obtained a loan from a family member to hire the professional lawyers/accountant that he desperately needs to try and understand and maybe challenge this Garnishee order that appeared 'out of nowhere'.

Note: under the Bankruptcy regime, a debtor with three dependents would not be required to contribute any income at all if they earned \$800 per fortnight (\$20,800 pa). A debtor in this situation would only be required to contribute if they earned more than \$74,810.74 net, and the required amount would be 50 cents in every dollar earned over the \$74,810.74 threshold.

The impact of administratively issued Garnishee orders

Pursuant to subsection 260-5(2) of Schedule 1 to the TAA, the ATO can issue a 'garnishee notice' and serve it on a third party that owes money or holds money for a tax debtor. This then requires the third party to pay an amount of money to the ATO, rather than paying it or continuing to hold it for the tax debtor. These notices are issued, and garnishing will occur upon the autonomous discretion of the ATO and does not require the parties to seek the order for debt enforcement via the courts. Debts owing to private sector creditors can only be enforced through a court process.

One of the central complaints raised by tax debtors who call the National Debt Helpline is the way in which ATO garnishee notices seem to appear 'out of the blue'. They feel as though they have not been 'heard out' or offered any avenues for a right of reply. A number of tax debtors expressed what they felt was an overall lack of transparency in the production of garnishee notices, as if this was a decision that was made behind closed doors and they have no choice but to agree. The process left debtors with an overall sense of powerlessness,

which left them resentful, and feeling as though they were at the mercy of the ATO's anonymous decision makers

One debtor (see case study below) explained that he felt as though he was constantly made to fear the lingering threat of a garnishee order, knowing that this order could be made and appear in full effect without any substantive notice. He criticised the way ATO employees raised the possibility of a future garnishee order in conversations with him and explained to us how this made him feel powerless to assert a claim which deviated from their narrative.

Another debtor who had previously been subjected to a private sector garnishee order (also below), explained he much preferred appearing before a court, telling us that he felt like he was able to adequately explain his circumstances and justify his debt. He resented that the ATO's s260-5 notice did not offer him this same 'day in court' where he could be heard out. It is conceivable that a formal judicial or mediation hearing, bringing together both debtor and ATO representative, would improve the creditor/debtor relationship and an improved sense of trust and respect from the public in the ATO as a public institution.

Case Study: James' story

James (not his real name) was fortunate in that owing to extensive negotiations with the ATO, he was not currently subject to a garnishee order. However, in our phone conversation with him, he spoke about what he viewed as the incessant, lingering threats that at any moment he might be garnished by the ATO. He told us that throughout the process he was constantly reminded that should he not comply with the ATO's directions, he could have his wages garnished.

James mentioned that he was being thrown in and out of panic due to what he perceived as threats, and how he used to worry about the flow on effects that such a garnishee order would have on his life, and how he would be able to pay rent from one month to the next. James told us that some of the harshest threats came from the hardship line, which he called hoping to speak to someone that would hear him out and at least empathise with his situation.

Importantly, James had received a garnishee order previously from a private creditor, and he explained to us that he felt the process of going to court and being heard out in a face to face setting was a much fairer experience. He was told that if the ATO so decided, they could slap a garnishee order on his wages at any point in time and that he wouldn't have any way to challenge it.

Case Study: Michael's story

Michael (not his real name) had his garnishee order removed from his and his wife's account after a great deal of negotiation with the ATO but explained that it took many tears and the right person on the other end of the line to reach an amicable solution to their tax debt. Michael's experience is important because he explained how, at the time of receiving the garnishee order, the order appeared without any prior notification consultation or warning. Michael was frustrated by the lack of a respectable or transparent process.

Suggestions for reform

Consumer Action acknowledges that the debt collection powers of the ATO post-bankruptcy may be necessary in the context of more complex corporate structures, where it is found that a demonstrable level of commercial financial literacy has been unethically applied to avoid the payment of large amounts of tax debt.



For example, the some \$20 million in debt accumulated by intertwining entities that was attempted to be recovered in the case of *Macquarie Health Corporation Ltd v FCT*. What we are suggesting is that garnishing income is a rather blunt instrument, and we recommend a more tailored approach to the use of such orders to avoid unnecessary and avoidable hardship. Small traders who make an honest mistake and are found to have breached their tax obligations should not be treated the same as more enterprising entities that strategically engage in tax avoidance. We note significant public concern around the ATO's debt collection practices focusing on 'easy target' small businesses and ill-equipped sole traders, rather than tackling larger, more sophisticated entities.¹¹

Our reform proposal therefore relies on a taxpayer income assessment like AFSA's indexed income assessment, that will entitle bankrupted small business and sole traders who earn less than a given threshold to receive their income free from garnishing. Where a bankrupted debtor's income exceeds the threshold, a percentage of their income may be garnished. However, if income does exceed this threshold and garnishment is to occur, this cannot occur simultaneously with other income contributions to the Official Trustee in a manner that worsens a person's situation and places them in dangerous financial difficulty.

Reform recommendation 1

Section 260-5 garnishee payments be suspended for small business/individuals and sole traders who earn below a given threshold. Garnishee payments may be reintroduced upon proof of earning above the threshold, but only incrementally, and only to an extent that when combined with income contribution to the Official Trustee the individual and their dependents still have an adequate amount of income.

We challenge the current process by which the ATO can rely on administrative powers to issue garnishee orders without any public proceedings. Debtors should be offered a formal hearing, whether this is to appear in a court or before some other administrative tribunal, whereby the debtor can explain their situation before an impartial decision maker. Our proposal would grant tax debtors right to natural justice.

Reform recommendation 2

The Tax Commissioner is no longer able to rely on administrative powers to issue garnishee orders in the absence of a public hearing. The Tax Commissioner should instead use the civil courts available to other creditors, or a judicial and/or administrative body should be appointed through which debtors can appear and present their claims.

We also propose an amendment to the maximum amount of income that can be garnished by the ATO and consider that this should be reduced from 30% to 20%, to avoid unnecessary hardship and the dangers of ongoing, deeper financial difficulty.

Reform recommendation 3

The maximum amount of income that can be garnished is reduced from 30% to 20%.

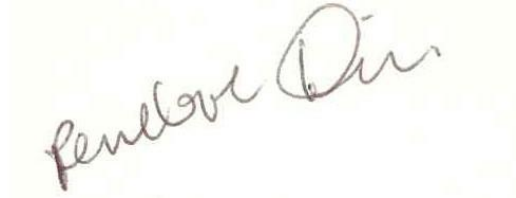
¹¹ ABC, 4 Corners, "Mongrel bunch of bastards", 9 April 2018.



Please contact Penelope Hill on 03 9670 5088 or at penelope@consumeraction.org.au if you have any questions about this submission.

Yours Sincerely,

CONSUMER ACTION LAW CENTRE

A handwritten signature in black ink on a light yellow background. The signature is written in a cursive style and reads "Penelope Hill".

Penelope Hill
Director – Financial Counselling

