PS LA 2011/7 - Settlement of debt litigation proceedings

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Practice Statement Law Administration

PS LA 2011/7

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SUBJECT: **Settlement of debt litigation proceedings**

PURPOSE: **To outline the relevant risk factors to be considered in bringing debt litigation proceedings to an end by settlement**

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BACKGROUND

1. The timely collection of taxation debts is predicated on an evaluation of risk to payment of these liabilities after they fall due.
2. Law Administration Practice Statement PS LA 2011/6 *Risk management in the enforcement of lodgment obligations and debt collection activities* outlines the Australian Taxation Office (ATO) risk management principles, as they apply to the collection of unpaid liabilities, having regard to the compliance model.
3. The compliance model reflects the different taxpayer attitudes to compliance and the corresponding compliance strategy that best responds to each particular attitude.
4. The level of risk in each case is assessed by applying that policy at the commencement of collection activities. In appropriate cases, the level of risk will warrant the commencement of litigation for recovery of an unpaid tax liability.
5. Once litigation for recovery has been initiated by or on behalf of the Commissioner, the risk assessment process continues throughout the litigation proceedings.
6. Where the relevant risk factors remain unchanged throughout the litigation proceedings, the Commissioner would generally pursue litigation to judgment and execution. However, at any time during litigation proceedings, additional facts may emerge or the debtor may advance submissions for settlement, which show upon reassessment of the risks involved that the level of risk warrants bringing litigation to an end.

TERMS USED

7. The following terms are used in this practice statement:

   Legal Services Directions 2005 (Legal Services Directions) – are the directions which the Attorney-General has issued under section 55ZF of the *Judiciary Act 1903*, providing guidance to agencies on a number of issues, including:

   - tied areas of Commonwealth legal work
   - the Commonwealth's obligation to act as a model litigant
   - handling monetary claims
   - the engagement of Counsel

- assistance to employees for legal proceedings

The Attorney-General's Legal Services Directions are legally binding on the Commonwealth agencies to which they apply, including the ATO. The Legal Services Directions help to ensure that Commonwealth agencies receive consistent and well coordinated legal services that are of a high standard, that uphold the public interest and that are sensitive to their context of Commonwealth interests which are broader than any one agency. (A link to the Legal Services Directions and information about the Directions is provided in the 'Other references' section at the end of this practice statement.)

Model litigant obligation – refers to the direction issued by the Attorney-General requiring that the Commonwealth and its agencies behave as model litigants in the conduct of their litigation. This requirement is set out in Appendix B to the Legal Services Directions. In essence, being a model litigant requires that the Commonwealth or one of its agencies, as a party to litigation, acts with propriety, fairness and in accordance with the highest professional standards. The obligation applies to the handling of civil claims and litigation before the Courts, Tribunals and Inquiries and in Alternative Dispute Resolution (ADR) processes. The model litigant obligation requires Commonwealth litigants to handle their cases efficiently and effectively in accordance with their responsibility to the community to deal responsibly with public revenue and also to fulfil their responsibilities to other litigants and the justice system.

Settlement – in the context of this practice statement, means deciding not to commence litigation on consideration of the relevant risk factors or ending litigation early due to new risk factors that have emerged after commencement of litigation.

Undisputed primary tax debt – refers to a debt which is not the subject of an objection, review or appeal under Part IVC of the *Taxation Administration Act 1953* (TAA).

Unpaid tax liability – includes reparation orders, legal costs and other liabilities that are payable to the Commissioner on behalf of the Commonwealth.

SCOPE

8. This practice statement should be read in conjunction with the ATO's *Code of settlement practice* (Code).

9. The Code sets out the ATO's official guidelines on the settlement of taxation disputes that arise under Part IVC of the TAA. It provides guidance as to the situations in which settlement of such disputes could be considered and outlines the processes which should be followed to settle such disputes.

10. Debt litigation proceedings has been expressly excluded from the scope of the Code because the Code concerns resolving what the correct liabilities and entitlements of a taxpayer are, while debt litigation proceedings are largely concerned with the recovery of debts due to the Commonwealth in relation to taxation and other liabilities and entitlements that arise under the various legislation administered by the Commissioner.

11. Notwithstanding this, the aim of this practice statement is to apply similar principles and philosophies to those of the Code to debt litigation proceedings.

STATEMENT

12. Law Administration Practice Statement PS LA 2009/9 *Conduct of ATO litigation and engagement of Legal Services Branch*[1] outlines the policies and guidelines to be followed in the conduct of ATO litigation and acknowledges the appropriate use of all dispute resolution techniques to minimise litigation and related costs.

13. Settlement is widely recognised as an effective means of resolving issues in dispute in certain cases, with the focus on controlling unnecessary costs while achieving a swift and satisfactory resolution for all parties without the need for protracted litigation.

14. In the context of debt litigation proceedings, this practice statement mandates a careful examination of the potential risks involved in reaching a settlement.

Types of debt recovery disputes

15. Disputes arising out of debt litigation may be classified into four broad categories.

16. The first category consists of those cases where the subject matter of the dispute could potentially give rise to an arguable defence by the defendant by virtue of the existence of a statutory defence regime. Such cases would include the following:

    - director penalty matters (relating to penalties incurred by directors of non-complying companies under Division 269 of Schedule 1 to the TAA and Division 9 of Part VI of the *Income Tax Assessment Act 1936* (ITAA 1936) for penalties due prior to 1 July 2010)
    - actions commenced by liquidators against the Commissioner in relation to unfair preferences or other voidable transactions,[2] and
    - cases where the Commissioner seeks indemnity from a company director pursuant to section 588FGA of the *Corporations Act 2001.*

17. The second category consists of those cases where the Commissioner is pursuing the recovery of a debt notwithstanding the fact that it is the subject of a dispute under Part IVC of the TAA. This is covered in greater detail in Law Administration Practice Statement PS LA 2011/4 *Recovering disputed debts*.

18. The third category consists of those cases where a bona fide defence by the defendant may exist based on the particular facts of the case; for example where, in a pay as you go (PAYG) matter, the defendant argues that they were not an employer for the purposes of the law or where the defendant argues that they were not a partner at the relevant time and therefore not liable for a partnership debt.

19. The fourth category consists of all other cases where there is essentially no scope for the defendant to sustain a bona fide defence or where the defence is without merit or frivolous having regard to the 'conclusive evidence' provisions afforded by the taxation laws (for example, section 177 of the ITAA 1936).

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[1] Note the Legal Services Branch has undergone a name change and from 1 July 2013 is called the Dispute Resolution Practice.

[2] Note that there will be instances where it will be appropriate to settle a voidable transaction claim without the need for a liquidator to apply to the court for an order. See Law Administration Practice Statement PS LA 2011/16 *Insolvency - collection, recovery and enforcement issues for entities under external administration.*

20. In addition, cases involving applications by taxpayers to set aside a judgment or a statutory demand may, on the merit of the particular case, fall into either the third or fourth category.

What constitutes a settlement?

21. According to the Code:[3]

> A settlement involves an agreement or arrangement between parties to finalise their matters in dispute in situations where it is in the best interests of the Commonwealth to do so. In the case of taxation disputes, special considerations arise because on one hand, the Commissioner's basic duty is to administer taxation law through assessing and collecting taxes and determining entitlements. However, on the other hand, the Commissioner also has an obligation to administer the taxation system in an efficient and effective way. Settlements usually involve the need to balance competing considerations and call for the application of discretion and good sense.

22. At their broadest, the terms 'settlement' or 'compromise'[4] are used interchangeably in the context of litigation to mean the resolution of a particular claim or dispute. In essence, resolving a dispute in the debt recovery context usually means bringing the legal proceedings to an end by agreement of the parties.

23. Following settlement, the legal proceedings may be discontinued or the parties may enter into a Deed reflecting 'Terms of Settlement' to enforce the settlement.

24. Many aspects of the ATO's policy which may assist in the resolution of disputed matters that arise in litigation are already well documented in other practice statements, for instance:

- accepting a payment arrangement by instalments which results in proceedings being discontinued or stayed (Law Administration Practice Statement PS LA 2011/14 *General debt collection powers and principles*)
- remitting the general interest charge (GIC) to finalise litigation (Law Administration Practice Statement PS LA 2011/12 *Administration of general interest charge (GIC) imposed for late payment or under estimation of liability*)
- discontinuing litigation to allow the debtor to either apply to the Department of Finance and Deregulation or the Minister for a waiver of their debt under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) or alternatively apply to the Commissioner for release from their debt under the release provisions in cases of serious hardship (Law Administration Practice Statement PS LA 2011/17 *Debt relief*)
- waiving the debt under Division 342 of Schedule 1 to the TAA to facilitate proceeds of crime matters (Law Administration Practice Statement PS LA 2011/10 *Waiver of tax-related liabilities in proceeds of crime matters*)

[3] At paragraph 2 of Part 1 entitled 'Purpose and scope of this Code'.
[4] Note that in the tax debt recovery context, 'compromise' has a different meaning as explained in Law Administration Practice Statement PS LA 2011/3 *Compromise of taxation debts*.

- discontinuing litigation where new evidence adduced during the proceedings establishes that the debt sought to be recovered is irrecoverable at law (PS LA 2011/17), and
- discontinuing litigation where the debtor's circumstances change during the proceedings and it becomes apparent that the debt sought to be recovered is uneconomical to pursue (PS LA 2011/17).

25. As noted earlier, the risk assessment process starts at the onset of litigation and continues right through to finalisation of the proceedings. At any time during litigation proceedings, additional facts may emerge or the debtor may advance submissions for settlement, which show upon reassessment of the relevant risk factors involved, that the level of risk warrants bringing the litigation proceedings to an end. Accordingly, for the purposes of these guidelines the discussion of '*settlement'* is limited to deciding not to commence litigation proceedings on consideration of relevant risk factors or ending the litigation proceedings early due to new or additional risk factors that have emerged after the commencement of the litigation proceedings.

Compromise

26. Generally, settlement in debt litigation proceedings will require the Commissioner to accept a lesser amount than the total value of the claim and/or to agree to a payment arrangement.

27. Law Administration Practice Statement PS LA 2011/3 *Compromise of taxation debts* deals with the compromise of taxation debts. 'Compromise' in this context means to accept a sum less than payment in full of any *undisputed* primary tax debt. The principles in PS LA 2011/3 apply to ***all*** such decisions and remain relevant in considering an offer that may arise in debt litigation proceedings, where a bona fide defence is not available.

28. It is recognised that the prescriptive processes and procedures outlined in PS LA 2011/3, which require the debtor to make a detailed formal written request for compromise, may not be sustainable in the context of debt litigation proceedings where rigid time frames need to be observed. Nevertheless, in view of the fact that the Commissioner's power to compromise a taxation debt has only been delegated to a limited number of ATO Senior Executive Service (SES) officers, a recommendation to accept a compromise offer would ordinarily necessitate adjournment of the proceedings to enable escalation of the offer to the appropriate SES officer. However, in certain circumstances where sufficient information is available which clearly indicates that a compromise offer should not be accepted, a decision to decline the offer can be made by the Commissioner's representative in the proceedings.

29. PS LA 2011/3 applies specifically to the compromise of '*taxation debts*'. Accordingly, actions commenced by a liquidator against the Commissioner in relation to an unfair preference or other voidable transaction are outside the scope of PS LA 2011/3.

Legal basis for settlement

30. The Code sets out in detail the legal basis for settlement. It is now well accepted that the Commissioner's powers of general administration are wide enough to encompass settlement of any matters on principles which reflect good management of the tax and superannuation systems, overall fairness and best use of ATO resources ('the good management rule').

31. In the context of debt litigation, the Commissioner is equally empowered to enter into settlements which reflect the good management rule.

32. Tax officers must follow the principles and guidelines outlined in this practice statement when exercising the Commissioner's powers of general administration. It is noted, however, that it is not possible to set out all the circumstances in which these powers may or may not be exercised. Each case has to be considered on its merits and on the basis of all the relevant facts. Tax officers must exercise their own judgment in arriving at an appropriate decision. The decision should be made in good faith and without bias.

Authority to settle

33. Traditionally debt recovery proceedings were conducted primarily in the State or Territory Courts. However in recent times, a number of debt recovery matters are also being conducted in the Federal Court as well as the Federal Circuit Court. Each of these Courts has different case management requirements including varying degrees of court mandated and/or supervised ADR. Many of the defended debt recovery proceedings each year are subject to court ordered ADR, ranging from informal case conferences to formal mediations.

34. In addition, most of the unfair preference and indemnity proceedings against directors to which the Commissioner is made a party each year are appropriate to be subject to ADR.

35. The Commissioner had previously delegated the power to settle debt litigation proceedings to a limited number of SES officers. Given the growing volume of defended debt litigation matters and the Courts' apparent desire to reduce their case lists through ADR processes such as mediation, the growing demand for ATO officers to be authorised to participate in ADRs has led to further delegation of the Commissioner's power to settle debt litigation proceedings to officers in the Dispute Resolution Practice (DRP). Such authority also extends to the settlement of pre-litigation matters, in appropriate cases, where the purpose of settling is to avert litigation and the costs associated therewith.

Alternative dispute resolution

36. PS LA 2009/9 recognises the importance of ADR and mandates the use of case management plans to promote increased consideration and use of ADR processes.

37. Depending on the circumstances, there is a range of ADR processes, including mediation, which could be used to assist in reaching settlement. The ATO Dispute resolution homepage is designed as an internal access point for ADR information including policies, procedures, support materials and useful external links. (A link to this homepage is included in the 'Other references' section at the conclusion of this practice statement.)

38. A full discussion of the policies and guidelines that tax officers must follow when attempting to resolve or limit disputes by means of ADR is set out in Law Administration Practice Statement PS LA 2013/3 *Alternative Dispute Resolution (ADR) in ATO disputes.*

39. Prior to attending an ADR in respect of debt litigation proceedings, the Commissioner's representative will notify all parties, including the mediator or

facilitator, of the Commissioner's policies which apply to an ADR of the matter, including any limitations on settlement of the particular matter.

Risk management in litigation

40. PS LA 2009/9 explains that the management of technical issues across the ATO, including litigation, is subject to the Enterprise Risk Management Framework.[5]

41. The *ATO risk matrices* provided in the Enterprise Risk Management Framework distinguish between different levels of risk - tactical, operational or enterprise - across the organisation. The matrices are designed such that risk can escalate upwards through each level depending on an evaluation and assessment of consequence and likelihood ratings. The risk matrices also reflect the level of effort that should appropriately go into risk assessment at each of those levels, and where the risks are most appropriately addressed.

42. All litigation matters are subject to the Strategic Internal Litigation Committee (SILC) process and regular call-overs.

43. The SILC process is essential to all litigation matters. It facilitates communication between all stakeholders and ensures that appropriate consultation takes place prior to the making of any key decisions or the adoption of strategies.

44. A SILC conference is a meeting between key internal stakeholders, organised by the DRP officer and convened at various critical stages of the litigation matter. Where appropriate, external legal service providers can also be invited to participate in key SILC conferences.

45. Given the high volume and factual nature of litigation arising in debt matters, the call-over process is usually limited to the more complex defended matters that are not suitable for summary proceedings or where the defendant has been granted leave to defend the proceedings. Notwithstanding this, once any matter is in litigation, the litigation team (usually the DRP officer in conjunction with the DRP Manager and the Debt case officer) must undertake its own risk assessment (separate from the call-over and high risk technical issues[6] process) to determine the level of the litigation risk associated with the case. This will assist the team to determine and apply the most appropriate litigation strategy.

46. Risk assessment is not optional and must be carried out in every case. This reflects the wider requirement that risk management underpins all ATO activities as provided under the Enterprise Risk Management Framework. Litigation arising in debt matters is of high volume and often relates only to a factual dispute limited in its application to the circumstances of the particular taxpayer. Therefore, this may substantially limit the revenue risk associated with such debt litigation.

47. Where a complex debt litigation matter carries a high level of revenue risk, the requisite risk mitigation strategy will need to be developed by the relevant stakeholders. PS LA 2009/9 explains the role and responsibilities for developing risk mitigation strategies for all strategic litigation matters.

48. Strict conformance with the processes outlined in PS LA 2009/9 is mandatory.

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[5] See PS CM 2003/02 *Risk and issues management* and associated corporate management procedures and instructions.
[6] See PS LA 2012/1 *Management of high risk technical issues and engagement of officers in the Tax Counsel Network.*

Risk based principles

49. General considerations in the risk assessment process which may be relevant to the decision to commence, continue and/or settle debt litigation proceedings (including preference and indemnity proceedings) may include:

- the overall good management of the ATO
- the application of the compliance model
- the best use of agency resources (for instance, section 15 of the PGPA Act)
- the application of the Attorney-General's Legal Services Directions 2005 (and in particular, the Model Litigant obligations)
- changes in the risk assessment of the litigation, and
- whether the litigation is suitable as a test case for a wider principle or issue which may include law clarification or identifying the need for legislative reform.

50. The ongoing consideration of the factors set out above in the risk assessment process may at any stage of the litigation result in a conclusion being reached that, in the circumstances as now known or understood, litigation ought to now be settled.

51. Accordingly, these settlement principles apply to situations where there has been a change to the relevant risk factors associated with the subject case. That change may include:

- factors that were overlooked in the initial risk assessment prior to litigation commencing, and/or
- new factors that have emerged after commencement of litigation.

52. In assessing potential changes to the relevant risk factors associated with a subject case, due consideration must be given to the recognised risks to business outcomes from the conduct of litigation. Those risks include:

- Legal risk
- Revenue risk
- Operational risk
- Compliance risk
- Reputational risk

53. As a general rule, in evaluating the level of litigation risk in the face of a settlement offer, the comparison of the cost of litigation to the likely return to the revenue should not on its own be the determining factor in deciding whether or not to accept a settlement. However, whilst a single risk factor may not, on its own, warrant consideration of a settlement, the weight of a combination of any of the risk factors may justify settlement.

Legal risk

54. Legal risk refers to risks arising from the uncertainty in the interpretation of legislation administered by the Commissioner, and in a commercial sense uncertainty or ambiguity in contracts entered into. Legal risks also include the specific risks that flow from the litigation process itself, including risks of breaching court and tribunal orders, breaching or being perceived to breach the Attorney-General's Legal Services directions, adverse comment from the

courts and tribunals as well as the risk of increased litigation. The exposure arising from legal risks range from one-off decisions with minor consequences to substantial consequences for the law and Commonwealth revenue.

55. This type of risk is prominent in cases where evidence disclosed during litigation establishes that the defendant may have an arguable defence against the claim which is the subject of the proceedings.

56. Legal risk will be the primary and often determining factor for most cases considered appropriate for settlement.

57. The level of legal risk will vary in degrees across a broad spectrum of cases between those that have an arguable defence with very little prospect of success through to those that are highly (although not conclusively) likely to succeed. For example, this type of risk could be present in a director penalty case where the evidence adduced does not conclusively meet the statutory defence but could influence the Court to give judgment against the Commissioner. In this type of case, it may make good sense to settle the case based on the prospect of success as advised by the ATO's legal representative.

Revenue risk

58. All litigation carries with it a risk of monetary loss. In ATO litigation, the revenue at risk may depend in part upon whether the dispute is factual and therefore limited in its application to the circumstances of the particular taxpayer or litigant, or whether it may have wider revenue consequences in terms of legal principle that may have widespread effect.

59. This type of risk may arise in a case where a novel or arguable defence has the potential to affect well-settled ATO processes or where the Commissioner's position on a particular matter has not yet been settled. An adverse decision on such a case could impact on many others and affect the ATO's ability to deliver our projected collection targets. Such risks would need to be carefully managed, and in certain circumstances, may result in a decision to continue litigation in the pursuit of judicial clarity to justify legislative intent or highlight the need for legislative amendment. Conversely, the existence of other risk factors may warrant settlement of the matter on its merits.

Operational risk

60. Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. The risks to be identified under this heading are diverse, including the capability and availability of the individuals involved in the litigation team to carry out their duties competently, and the capabilities of internal and external systems to support the litigation in unusual and unforseen circumstances. Operational risks can be as obscure as bad weather stopping a key witness from attending court.

Compliance risk

61. Compliance risk is an acknowledgment that a number of key factors can influence taxpayer behaviour in complying with the law. It is the current and prospective risk to revenue arising from community non-conformance with laws, regulations, precedential ATO views (such as public rulings), or

standards of conduct normally expected of the community. Compliance risk also arises in situations where the law or ATO view expressed in precedential products may be ambiguous or untested. In this sense compliance risk is closely aligned with legal risk. The risk exposes the Commonwealth to loss of revenue. A case in litigation that potentially exposes a defect in tax law can have widespread consequences for compliance by the community and confidence in the system.

Reputational risk

62. Reputational risk refers to the negative experiences or perceptions that may arise during or as a result of litigation that may affect the ATO's standing with government, the judiciary, other Government agencies, our external advisers, or the community.

63. The decision as to whether or not to settle can, in certain circumstances, carry a reputational risk where the community perception is that the ATO is being 'too hard' or 'too soft' on certain taxpayers or market segments. Similarly there are reputational risks if settlements are not seen to be applied consistently.

64. Community confidence in the ATO could also be jeopardised by perceptions of prejudice and disadvantage to those taxpayers who meet their payment obligations by the due date, if the Commissioner were to settle litigation with taxpayers who have not engaged with the ATO to meet their obligations.

65. To settle in such circumstances would undermine the ATO compliance model and could expose the ATO to the reputational risk of failing to meet its statutory obligations. Such risk has the potential to diminish community confidence and impact on the reputation of the ATO.

Commercial settlement

66. During litigation, the defendant may offer payment of an amount which exceeds the net value of their assets or an amount that exceeds the net maximum return after accounting for an estimate of the Commissioner's costs of continuing the litigation.

67. This type of settlement offer is often referred to as a 'commercial settlement', where the proposed return is aimed at minimising exposure to the costs associated with the continuation of litigation and returning an amount greater than would ultimately be collected at the conclusion of litigation.

68. PS LA 2011/3 discusses commercial settlements and conveys the principle that 'the Commissioner will not accept compromise proposals unless there is a benefit in doing so over and above the returns that would flow from taking either bankruptcy or corporate insolvency actions'. That practice statement provides that the Commissioner will not take into account the additional costs of litigation which are caused by the debtor failing to engage with the Commissioner earlier. Only the reasonable future costs of litigation and asset realisation can be taken into account.

69. As a general rule, a 'commercial settlement' will only be accepted in limited circumstances. The rationale is that a personal insolvency agreement or debt agreement under the *Bankruptcy Act 1966* or in the case of a corporate insolvency, a voluntary administration under Part 5.3A of the *Corporations Act 2001,* is considered to be more appropriate in terms of fairness to all creditors and also for certainty in terms of disclosure about asset holdings.

70. Notwithstanding this, a commercial settlement may be warranted in circumstances where in addition to the commercial aspect of the offer, there are other relevant risk factors present that warrant settlement.

When settlement discussions may occur

71. In debt litigation proceedings, settlement discussions between the Commissioner and taxpayers will generally take place after commencement of the proceedings, usually after lodgment of a defence. However, in certain circumstances, taxpayers may wish to minimise their legal costs by making settlement overtures prior to formally lodging a defence.

72. In cases involving voidable transactions, a liquidator will generally commence negotiations for settlement immediately after serving the Commissioner with a letter of demand which provides sufficient evidence of the claim but prior to the issue of legal proceedings under section 588FF of the *Corporations Act 2001* in cases where a settlement cannot be reached without proceeding to litigation.

73. Where a settlement offer is received after the commencement of the litigation proceedings, the DRP officer or external legal service provider will confer with the Debt case officer to determine whether there has been any change to the relevant risk factors assessed prior to the commencement of these proceedings that warrants bringing the litigation proceedings to an end by settlement.

74. Similarly, in other matters where legal proceedings are imminent but have not yet been commenced by the ATO, such as director penalty matters, representations to settle the matter may be received with the view to avert litigation. The guidelines set out in this practice statement will generally apply where a case lends itself to settlement upon assessment of litigation risks. However, where it is proposed to accept an offer for a lesser sum than the full amount of the primary tax, based on considerations other than litigation risks, the matter should be dealt with in accordance with the compromise guidelines set out in PS LA 2011/3.

75. In a number of circumstances, particularly in cases where a bona fide defence may not be available, although the risks assessed may remain unchanged, taxpayers may wish to end litigation by entering into a repayment arrangement or negotiating a compromise. Settlement in those circumstances may well be acceptable having regard to the guidelines set out in other law administration practice statements.

76. In cases involving litigation for recovery of debts which are the subject of a dispute under Part IVC of the TAA, settlement may also be appropriate subject to the mitigation of the risks originally assessed with regards to the considerations laid out in the Code and in Law Administration Practice Statement PS LA 2011/4 *Recovering disputed debts*. Consultation with the case officer dealing with the Part IVC dispute would be paramount in considering any offer of settlement.

Circumstances where it may be generally appropriate to settle

77. As a general guide, settlement may be an appropriate way to resolve a matter if:

- there is doubt about the Commissioner's ability to overcome the taxpayer's defence and the costs and time delay associated with collecting the full amount of the debt are such that the real value of the

proposed settlement offer is in excess of the amount that is likely to be collected some time in the future

- scope exists for the matter to be resolved swiftly through ADR without expending further costs in continuing to defend or pursue a claim
- there is insufficient evidence available (for example, through the passage of time) to support the Commissioner's ability to successfully recover funds held by entities other than the taxpayer, or
- pursuing a matter to trial could prejudice well-established principles of law.

78. Where fresh evidence which comes to light during the proceedings clearly establishes and supports the taxpayer's defence, the Commissioner, as a model litigant, would be required to discontinue the litigation.

Circumstances where it would be generally inappropriate to settle

79. As a general guide, it would be inappropriate to settle in circumstances where:

- the outcome of the settlement would be contrary to an articulated policy reflected in the law
- the matter is subject to escalation to settle the ATO view
- the inability to pay the tax debt has been deliberately contrived through the dissipation of assets to third parties
- the taxpayer's defence is poor and unlikely to be pursued through to trial. Care is necessary to ensure the settlement practice does not encourage frivolous defences
- it is in the public interest to have judicial clarification of the issue and the case is suitable for this purpose – in such cases, it may be appropriate to fund the litigation under the test case litigation program[7]
- the matter is beyond challenge or there is a clearly established and articulated precedential ATO view on the issue or precedential authority in favour of the Commissioner already exists
- the settlement would involve inconsistency of treatment for taxpayers in comparable circumstances, or
- litigation of the matter through the courts could have a significant flow-on compliance effect and the case is suitable for this purpose.

Remission of GIC

80. The ATO policy governing the remission of GIC is set out in PS LA 2011/12 *Administration of general interest charge (GIC) imposed for late payment or under estimation of liability.* This practice statement mandates that remission of GIC is not to be used as an inducement to settle a disputed debt, though, in certain circumstances, remission of GIC may form a component of a settlement.

[7] Under the test case litigation program, the ATO provides financial assistance to taxpayers whose litigation 'is likely to be important to the administration of Australia's revenue and superannuation system'. The criteria for applying for test case funding are available on the ATO website at www.ato.gov.au.

Settlements and prosecutions

81. Care needs to be exercised in considering settlement offers in debt litigation proceedings where the debtor is the subject of a prosecution or is in the process of being charged with criminal offences.

82. Guidelines and procedures for referring cases to Serious Non-Compliance (SNC) can be found in Chief Executive's Instruction CEI 2014/05/09 *Tax Crime and External Fraud* and associated documents. If a case falls within the guidelines, tax officers should seek a formal written response from SNC on the impact of a settlement on a potential prosecution before entering into any settlement negotiations. In providing the written response, SNC will normally seek advice from the Commonwealth Director of Public Prosecutions (CDPP) on the issue.

83. Tax officers should also formally advise SNC if there are indications that criminal offences may have been committed by the taxpayer and/or another party. SNC will then provide advice, including what action, if any, that SNC may take.

84. SNC will consider the question of prosecution or other responses including, if appropriate, the referral of the matter to the CDPP in respect of criminal prosecutions.

85. Where a matter has been referred to SNC or the Australian Federal Police, tax officers must formally advise SNC of any proposed settlement before taking any action which might prejudice any investigation.

No prosecution exemption

86. Tax officers do not have authority to make it a condition of a settlement that a taxpayer or another person will not be prosecuted, or that proceedings associated with a prosecution will not be taken either by the ATO or another agency. Accordingly, a clause or condition that purports to exempt a taxpayer or another party from prosecution, or associated proceedings, cannot form part of any ATO settlement agreement and is not enforceable.

87. Equally, it is ATO policy that tax officers must never use the threat of prosecution, either actual or implied, as a lever to settle cases.

Procedures

88. To ensure transparency, consistency and accountability, strict compliance with the DRP procedures for settlement is mandatory.

89. For staff development and quality assurance as well as corporate governance purposes, settlements accepted by the ATO may be selected for the integrated quality framework process which will be conducted jointly by senior officers of Service Delivery (Debt) and Dispute Resolution Practice.

Amendment history

Date of amendment	Part	Comment
28 November 2013	Various	Revised to: meet current ATO Style guide requirements; reflect new work group titles
	Various	To reflect current practices in relation to voidable preference type of litigations
	Various	Revised to cater for amendments to PS LA 2009/9.
3 July 2014	Paragraphs 24; 49; 82 & 84; legislative references	Updated references to *Financial Management and Accountability Act 1997* with relevant provisions in the *Public Governance, Performance and Accountability Act 2013* and *Public Governance, Performance and Accountability Rule 2014;* updated references to PS CM 2007/02 now replaced by CEI 2014/05/09;

ATOLaw topic	Income Tax ~~ Administration ~~debt recovery and insolvency
Legislative references	ITAA 1936 177 ITAA 1936 Pt VI Div 9 TAA 1953 Pt IVC TAA 1953 Sch 1 Div 269 TAA 1953 Sch 1 Div 342 Bankruptcy Act 1966 Corporations Act 2001 588FGA Corporations Act 2001 588FF Corporations Act 2001 Pt 5.3A PGPA Act PGPA Act 15 Judiciary Act 1903 55ZF
Related practice statements	CEI 2015/03/01 Risk management PS LA 2009/9 Conduct of ATO litigation and engagement of ATO Dispute Resolution PS LA 2011/3 Compromise of undisputed tax-related liabilities and other amounts payable to the Commissioner PS LA 2011/4 Collection and recovery of disputed debts PS LA 2011/6 Risk management in the enforcement of lodgment obligations and debt collection activities PS LA 2011/10 Waiver of tax-related liabilities in proceeds of crime matters PS LA 2011/12 Remission of General Interest Charge PS LA 2011/14 General debt collection powers and principles PS LA 2011/16 Insolvency – collection, recovery and enforcement issues for entities under external administration PS LA 2011/17 Debt relief, waiver and write off PS LA 2012/1 Engagement of Tax Counsel Network on high risk technical issues PS LA 2013/3 Alternative Dispute Resolution (ADR) in ATO disputes
Other references	Code of settlement Alternative Dispute Resolution (ADR) homepage (internal link only) Legal Services Directions 2005 CEI 2014/05/09 *Tax Crime and External Fraud* (internal link only)
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