



**Australian Government**  
**Inspector-General of Taxation**

# **Review into the ATO's compliance approaches to small and medium enterprises with annual turnovers between \$100 million and \$250 million and high wealth individuals**

## **Report to the Assistant Treasurer**

**Inspector-General of Taxation**

**December 2011**

© Commonwealth of Australia 2011

ISBN 978 0 642 74779 2

## Ownership of intellectual property rights in this publication

Unless otherwise noted, copyright (and any other intellectual property rights, if any) in this publication is owned by the Commonwealth of Australia (referred to below as the Commonwealth).

## Creative Commons licence

With the exception of the Coat of Arms (see below), the IGT logo and ATO sourced material, this publication is licensed under a Creative Commons [Attribution 3.0 Australia](http://creativecommons.org/licenses/by/3.0/au/deed.en) Licence.



Creative Commons Attribution 3.0 Australia Licence is a standard form licence agreement that allows you to copy, distribute, transmit and adapt this publication provided that you attribute the work. A summary of the licence terms is available from

<http://creativecommons.org/licenses/by/3.0/au/deed.en>. The full licence terms are available from <http://creativecommons.org/licenses/by/3.0/au/legalcode>.

The Commonwealth's preference is that you attribute this publication (and any material sourced from it) using the following wording:

Source: Licensed from the Australian Government Inspector-General of Taxation under a Creative Commons [Attribution 3.0 Australia](http://creativecommons.org/licenses/by/3.0/au/deed.en) Licence.

The Australian Government Inspector-General of Taxation does not necessarily endorse third party content of this publication.

## Use of the Coat of Arms

The terms under which the Coat of Arms can be used are set out on the It's an Honour website ([see www.itsanhonour.gov.au](http://www.itsanhonour.gov.au))



Telephone: (02) 8239 2111  
Facsimile: (02) 8239 2100

**Australian Government**  
**Inspector-General of Taxation**

Level 19, 50 Bridge Street  
Sydney NSW 2000  
GPO Box 551  
Sydney NSW 2001

16 December 2011

Senator the Hon Mark Arbib  
Assistant Treasurer, Minister for Small Business, Minister for Sport  
Parliament House  
Canberra ACT 2600

Dear Minister

**Review into the Australian Taxation Office's (ATO) compliance approaches to small and medium enterprises with annual turnovers between \$100 million and \$250 million (larger SMEs) and high wealth individuals (HWIs)**

I am pleased to present you with my report on the above review. The review was conducted in response to concerns raised by taxpayers, tax practitioners and their representative bodies following the ATO's increased compliance focus on larger SMEs and HWIs pursuant to its commitment to Government.

Taxpayers' concerns related to unfair treatment and unnecessary compliance costs stemming from the wide scope of ATO information gathering requests, delays as well as a lack of commercial awareness, technical knowledge and conduct of ATO staff. The underlying issue seemed to be a lack of ATO staff capability servicing this market segment.

The ATO has acknowledged the need for improvements to deal with these concerns and since the commencement of the review, it has worked with my office to fashion a significant program of work.

I have made 41 recommendations some of which reinforce the work that the ATO has already begun whilst others are more distinct but complimentary to that work. The ATO has agreed in full with 38 of my recommendations, two in part and disagreed with one.

The implementation of these recommendations together with the program of work already commenced by the ATO should result in significant improvements in this area of tax administration. However, these improvements may not become apparent immediately as staff capability, for example, may take some time to develop.

I offer my thanks for the support and contribution of taxpayers, tax practitioners and their representative bodies to this review. The willingness of many to provide their time in preparing submissions and discussing issues with myself and my staff is greatly appreciated. I also thank the relevant ATO officers for their professional cooperation and assistance in this review.

Yours faithfully

Ali Noroozi  
Inspector General of Taxation



# TABLE OF CONTENTS

<b>EXECUTIVE SUMMARY .....</b>	<b>1</b>
<b>CHAPTER 1 — BACKGROUND.....</b>	<b>3</b>
Conduct of review .....	3
What are SME, HWI and WA taxpayers? .....	5
Key differences between the larger SME and large business market segments .....	5
The ATO's compliance approach to SMEs, HWIs and WAs .....	6
Key differences in type of ATO support .....	7
Transforming Tax Technical Decision Making (TTTDM) Project .....	8
Additional government funding .....	9
<b>CHAPTER 2 — TECHNICAL CAPABILITY AND SUPPORT.....</b>	<b>13</b>
Complexity of case work in the S4 market segment .....	14
Staff understanding of the end-to-end process .....	16
Level of staff capability .....	18
The characteristics of expert compliance officers .....	29
SME business line's three-year capability aspirational target .....	32
Specialisation .....	32
Numbers of staff turnover .....	33
Staff engagement.....	37
Recruitment — perceptions of SME business line positions .....	38
Staff retention strategies .....	39
Staff training and capability development .....	40
<b>CHAPTER 3 — COMPLIANCE DECISION-MAKING .....</b>	<b>49</b>
Risk identification and case selection .....	50
Level of disputation .....	51
HWI objection work .....	54
Consideration of Part IVA issues .....	56
Evasion .....	57
Improving officers' technical discipline — use of the Facts and Evidence Worksheet.....	58
Integrated Quality Framework's (IQF) assurance of work quality.....	62

<b>CHAPTER 4 — PROJECT MANAGEMENT</b>	<b>65</b>
Government funding and ATO allocations	65
Increased technical resources	66
Active compliance case end-to-end reporting	67
Cycle times for ATO activities	68
HWI taskforce workflows	71
Income Tax Investment (ITI) — S4 market segment workflows	73
Wealthy Australians (WA) Project	74
Project management of cases	75
Systems support	76
Interpretative Assistance (IA) area’s resourcing	77
Change management	81
<b>CHAPTER 5 — AUDIT CONDUCT, COMMUNICATION AND TAXPAYER ENGAGEMENT</b>	<b>83</b>
Expectations and escalation processes	83
Opening meetings for compliance activities	86
Allowing tax advisers to be more effective	87
Discussion with taxpayers before views are documented in writing	88
Changing the basis for amendments	89
Changing auditors during compliance activities	90
Communicating commencement and finalisation of compliance activities	91
<b>CHAPTER 6 — INFORMATION GATHERING</b>	<b>93</b>
Setting expectations in information gathering	94
Asymmetries in timeframes	95
Private group structure questionnaires	96
Information gathering initiatives	97
<b>APPENDIX 1 — TERMS OF REFERENCE AND SUBMISSION GUIDELINES</b>	<b>99</b>
<b>APPENDIX 2 — HWI OBJECTIONS WORKLOADS</b>	<b>104</b>
<b>APPENDIX 3 — ATO-IDENTIFIED AREAS FOR IMPROVEMENT</b>	<b>105</b>
<b>APPENDIX 4 — CHARACTERISTICS OF EXPERT COMPLIANCE OFFICERS: EXTRACT FROM     INSIDE STORY’S REPORT</b>	<b>109</b>
<b>APPENDIX 5 — ATO RESPONSE</b>	<b>111</b>
<b>LIST OF RECOMMENDATIONS</b>	<b>113</b>
<b>GLOSSARY</b>	<b>127</b>

## EXECUTIVE SUMMARY

The Australian Taxation Office (ATO) identifies small and medium sized enterprises with annual turnovers between \$100 million to \$250 million (larger SMEs) as a particular compliance focus. There are approximately 1400 larger SMEs, over half of which are controlled by individuals with more than \$30 million in net wealth. Such individuals are referred to as high wealth individuals (HWIs) by the ATO.

The Inspector-General of Taxation (IGT) conducted this review in response to concerns raised by taxpayers, tax practitioners and their representative bodies as a result of an increased ATO compliance focus on larger SMEs and HWIs. These taxpayers believed they were unfairly treated and subject to unnecessary compliance costs. The specific concerns related to the ATO's wide scope of information requests, delays, staff conduct in audit and their lack of commercial and technical knowledge. The overarching theme seemed to be a lack of staff capability.

In this review, the IGT has identified key opportunities for improvement in a number of areas, including: technical capability and support; initial compliance decision making; project management; audit conduct, communication and engagement; and information gathering.

Technical capability and support – Many concerns identified in this review would be resolved by improving staff technical capability. Larger SME and HWI matters are often highly complex and the need for lead times in capability development is appreciated. Importantly, once developed that capability must be maintained. The ATO's senior management has recognised both the SME business line's significant staff capability challenges arising over the next few years and the need to address it. Accordingly, the IGT has made a number of recommendations including:

- better matching the complexity of case work with officers' training and experience;
- clearly defining roles and responsibilities of relevant ATO officers;
- reinforcing the role of the ATO's Senior Technical Leadership;
- improving ATO approaches to recruiting and developing compliance officers;
- facilitating a degree of compliance officer specialisation;
- improving ATO officers' understanding of commercial and business issues; and
- strengthening staff training including the involvement of external experts.

Initial compliance decision making – The ATO has sought to improve initial ATO compliance decisions in the larger SME and HWI areas. However, there is scope for further improvement in a number of areas and the IGT has made a number of recommendations including:

- improving the interpretative assistance area's resourcing and engagement with the active compliance area;
- using the Facts and Evidence Worksheet to develop technical positions; and
- developing better understanding of the rejection of initial compliance decisions.

Project Management – The IGT has identified project management as an area for improvement. The IGT recommendations requiring ATO management action will greatly enhance transparency and accountability in this area.

Audit conduct, communication and engagement – During the review, the ATO agreed to extend the scope of its *Wealthy and wise* booklet from HWIs to the entire SME market segment. The IGT welcomes this initiative as the booklet provides stakeholders with better understanding of the process and a means of holding ATO officers to account where expectations are not met. The IGT has also identified a number of additional areas to be covered in the booklet including:

- communicating the start and end of compliance actions;
- allowing tax advisers the opportunity to review clients' affairs;
- escalation processes; and
- discussions with taxpayers before adverse ATO views are documented.

Information Gathering – The direct and opportunity costs for taxpayers stemming from ATO information gathering and related compliance action was a very significant area of concern to taxpayers and their advisers. The IGT has concluded that better ATO management of information in their dealings with taxpayers and advisers should assist in minimising delays and compliance costs. It should also assist in reducing perceptions of unfairness. The ATO's commitment to improved engagement with taxpayers and their advisers on information requests should also improve the overall stakeholder relationship and experience.

In conclusion, the ATO has acknowledged the need for improvements in the above areas and, since the commencement of the review, has worked with the IGT to fashion a significant program of work. In this review, the IGT has also made 41 recommendations some of which reinforce the work that the ATO has already begun whilst others are more distinct but complimentary to that work. The ATO has agreed in full with 38 of these recommendations, two in part and disagreed with one.

The appropriate implementation of the recommendations in this review together with the program of work already commenced by the ATO should result in significant improvements in this area of tax administration. However, these improvements may not become apparent immediately as staff capability, for example, may take some time to develop.



# CHAPTER 1 — BACKGROUND

## CONDUCT OF REVIEW

1.1 This is the Inspector-General of Taxation's (IGT) report of his review into the Australian Taxation Office's (ATO) compliance approaches to small and medium enterprises with annual turnovers between \$100 million and \$250 million (larger SMEs or S4 taxpayers) and high wealth individuals (HWIs). The report is produced pursuant to section 10 of the *Inspector-General of Taxation Act 2003* (IGT Act 2003).

1.2 This review was commenced pursuant to subsection 8(1) of the IGT Act 2003 and in response to submissions from concerned taxpayers and their representatives. The concerns generally related to taxpayers not receiving fair and equitable treatment and being unduly burdened with unnecessary compliance costs stemming from the wide scope of ATO information gathering requests, delays, lack of commercial awareness and technical knowledge, as well as conduct of ATO staff. The underlying issue seemed to be a lack of staff capability in this market segment.

1.3 Particular concerns were raised with the implications of certain ATO announcements made from late 2008. These announcements explained that as a result of additional funding from the Government, the ATO would:

- expand its compliance activities to risk assess over a four-year period all larger SMEs, and follow this work up with more reviews and audits; and
- increase its monitoring, reviews and audits of HWIs.<sup>1</sup>

1.4 Stakeholders commented that the ATO's recent compliance focus on the larger SME and HWI market segments was understandable. However, they considered the increased focus entailed a significant execution risk because the ATO had a general capability shortfall in this sector. They considered that the additional ATO compliance focus would significantly increase unnecessary costs and workloads for both taxpayers and the ATO, unless some improvements were realised.

1.5 Terms of reference were announced on 7 April 2010 for this review. Appendix 1 reproduces a copy of the terms of reference and submission guidelines for this review.

1.6 The IGT received over 30 submissions from taxpayers and their representatives. The IGT also met with interested taxpayers, their representatives and selected industry and tax practitioner bodies to understand their experiences.

---

1 Australian Taxation Office, *2008–09 Compliance Program*, Canberra, 2008, p. 37.

1.7 A number of submissions expressed concerns with the ATO's approach to individuals with net wealth of between \$5 million to \$30 million (Wealthy Australian taxpayers or WAs). During initial inquiries, it became apparent that the ATO's work in the WA market segment was integral to the underlying issues examined in this review. The IGT therefore incorporated consideration of the ATO's WA activities insofar as they were relevant to considering the underlying issues of concern that initiated this review.

1.8 Work on this review was largely put on hold between April and December 2010 whilst the IGT diverted its limited resources to conduct a review into the ATO's Change Program at the direction of the then Minister. The review into the ATO's Change Program commenced immediately after the Minister's direction, dated 19 April 2010, due to the urgency of the matters requiring review and the public interest in those matters. Work on this review, that is, the ATO's compliance approaches into larger SMEs and HWIs, recommenced in early 2011 after the Change Program review had been completed.

1.9 During the review, the ATO advised the IGT that the area responsible for dealing with larger SMEs and HWIs – the SME business line – was moving towards reviewing economic groups (the 'private wealth' approach), focusing on building staff capability and collective support and setting key aspirational targets on qualitative and procedural measures. Significant work is underway.

1.10 If implemented effectively over the appropriate time frame, the results of these ATO initiatives should go some way towards reducing external stakeholders' current concerns. However, the work the ATO is undertaking in this regard may need some fine tuning as it progresses. In responding to stakeholder concerns, the IGT also considers that there is scope for further improvement in a number of important areas as set out in the chapters that follow.

1.11 To assist with the IGT's consideration of issues, the IGT established a working group comprising key tax practitioners and representatives: John Brazzale, Pitcher Partners; Lance Cunningham, PKF; David Drummond, KPMG; Keith James, Hall and Wilcox; Ken Schurgott, Schurgott Noolan Pty Ltd; Glenn Williams, Ernst & Young; and senior ATO officials.

1.12 The IGT greatly appreciates the generosity of the members of this working group in freely giving their time and expertise. Their involvement has greatly enhanced the outcomes of this review.

1.13 The working group met several times to discuss the potential solutions to the systemic issues identified in this review. It should be noted, however, that the views and recommendations expressed in this report are not necessarily those of individual members of the working group. The views and recommendations were finalised by the IGT after much deliberation, and based on input received and discussions with private sector representatives and the ATO.

1.14 The IGT also worked progressively with ATO senior management to distil the scope for improvement and to agree on specific actions. The IGT also discussed these matters with interested external stakeholders and working group members.

1.15 In accordance with section 25 of the IGT Act 2003, the Commissioner of Taxation was provided with an opportunity to make submissions on any implied or actual criticisms contained in this report.

## **WHAT ARE SME, HWI AND WA TAXPAYERS?**

1.16 SMEs range from very simple businesses with high turnovers to businesses with complex structures involving multiple entities and complex tax issues. Included in this range are those businesses with turnover between \$100 million and \$250 million (that is, S4 taxpayers).

1.17 Since 2008, the ATO has classified SMEs as those entities having between a \$2 million and \$250 million turnover. The ATO estimates that there are around 175,000 such entities. HWIs also feature in this market segment, with the ATO estimating more than 2660 such individuals who, with associates, effectively control more than \$30 million in net wealth each.<sup>2</sup>

1.18 The SME market segment pays approximately 15 per cent of the total tax that the ATO collects and a further 12 per cent is withheld by SMEs on behalf of their employees. More than 28 per cent of employees in Australia work for SMEs.<sup>3</sup>

1.19 Recently, the ATO has also focussed its efforts on WAs. The ATO estimates that there are more than 82,000 WAs, who between them control in excess of 400,000 entities.<sup>4</sup>

## **KEY DIFFERENCES BETWEEN THE LARGER SME AND LARGE BUSINESS MARKET SEGMENTS**

1.20 There are a number of key differences between S4 taxpayers (particularly entities that are part of a closely held private group (CHPG)) and large businesses.

1.21 Large businesses tend to be public companies. This means that:

- more information about the company, its operations and finances are publicly available, whereas more than half of larger SMEs are part of CHPGs meaning that there is less publicly available information compared to that of public companies;
- its internal structure and governance processes are more transparent, whereas CHPGs tend not to have the same level of transparency and may use some form of trusts to conduct business (issues of trusts being complex and numerous);

---

2 Australian Taxation Office, *Compliance Program 2011–12*, Canberra, 2011, pp. 16–17.

3 Australian Taxation Office, *Compliance Program 2009–10*, Canberra, 2009, p. 18.

4 Australian Taxation Office, *Compliance Program 2011–12*, Canberra, 2011, p. 18.

- executive control and access to the business' wealth is more removed, whereas as executive control of a CHPG's finances may have more of an emotional attachment; and
- there may be a greater resourced in-house tax function, whereas larger SMEs may have less resources and therefore seek tax advice as and when thought needed.

## **THE ATO'S COMPLIANCE APPROACH TO SMEs, HWIs AND WAS**

1.22 In 2010–11, the ATO had a total operating expenditure of \$3.1 billion and employed 22,667 staff (not including the pool of around 2500 casual employees that the ATO can call on during times of peak workloads).<sup>5</sup> The ATO allocates a substantial proportion of this budget to its activities aimed at assuring compliance with the tax laws (the compliance program).

1.23 The ATO's compliance program is delivered by a number of different business units whose focus is determined by the type of taxpayer, revenue product or risk assigned to it.

### **The SME business line**

1.24 For 2010–11, the SME business line was responsible for compliance activities in relation to the following areas:

- SMEs (broken up into four market segments – the most relevant segment for this review is the S4 market segment);
- HWIs;
- WAS (in conjunction with the ATO's Micro Enterprises and Individuals (MEI) business line);
- non-profit organisations;
- government entities; and
- the fringe benefits tax product.

1.25 On an annual basis, the SME business line develops compliance strategies in relation to its areas of responsibility and in accordance with a range of expectations set by ATO corporate plans, compliance program plans and commitments to government.

1.26 There are 15 senior ATO officers tasked with providing strategic leadership to the SME business line. These strategies are outlined in the ATO's *Compliance Program*, which is published each year. The SME Executive tracks delivery of these strategies on

---

<sup>5</sup> Commissioner of Taxation, *Annual Report 2010–11*, Canberra, 2011, p. 9.

a monthly basis. Contributions to the ATO's compliance sub-plan are reported periodically to the Compliance sub-plan's committees.

1.27 The 2010–11 budget for the SME business line was \$153.6 million for a total full-time equivalent (FTE) staff of 1492.5 in number.

1.28 As at 30 June 2010, the SME business line employed approximately 1445 staff, comprising 145 staff working in governance and support roles, 247 staff in Interpretative Assistance (IA), 953 staff in Active Compliance (AC) and 100 staff in compliance risk and intelligence.

1.29 For the 2010–11 year, the SME business line allocated a total of 832.6 FTE staff to its 2011 compliance strategies. Of this amount, the SME business line allocated:

- 127 FTE staff to S4 work (94 FTE staff allocated to the ITI funding work and 33 FTE staff allocated to other risk work in the S4 market segment — note that a combination of the two is what the SME business line reports as its Income Tax Investment (ITI) commitment to Government);<sup>6</sup>
- 324.4 FTE staff to HWI work; and
- 94 FTE staff to WA work.<sup>7</sup>

1.30 This FTE staff allocation represents the expected workload of 2011 active compliance activities for these strategies. It does not mean that 545.4 staff have been allocated to work exclusively on these strategies, but that just under two-thirds of the total SME active compliance workload will comprise HWI, S4 and WA work.

## **KEY DIFFERENCES IN TYPE OF ATO SUPPORT**

1.31 There are also a number of key differences in the support the ATO provides to its officers in the SME business line and the Large Business and International (LBI) business line:

- SME officers could potentially work on a CHPG, a public group as well as a friendly society. The LBI business line utilises specialisation far more and is accordingly able to gain a more intimate knowledge of a taxpayer's business environment and associated tax risks.
- The LBI and HWI areas have more established linking systems, whereas the SME business line is relying on a linking system (BMT) that may not be identifying all relevant linked-entities (discussed in chapter 4).

---

6 See 'S&ME Active Compliance — performance report: year to date 24 February 2011', p. 5, reported to the SME Executive.

7 Mid-Year Review SME 2011 Internal Plan; Note also that the SME's information collection teams may also carry out specific work on HWI, WA and S4 taxpayers — these figures are not included as their work is preliminary to conducting reviews and audits and do not directly result in liabilities and collections.

- Both the LBI and HWI areas have more direct time available in a Preliminary Risk Review (PRR) and have longer cycle times in a Comprehensive Risk Review (CRR).

1.32 A recently commissioned internal ATO report that reviewed aspects of the SME business line considered the potential for further SME and LBI business line interaction, amongst other things. It observed that:

There may be advantages in further exploring the ways S&ME [the SME business line] currently interact with the technical networks in LB&I [the LBI business line]. These networks attempt to share capability and provide on the job training across AC and IA areas ...

... Furthermore, there are advantages that can be gained from BSLs [the ATO's business lines] sharing approaches that leverage off functional areas. Currently, SM&E and LB&I work closely together and share opportunities to develop staff across these functional areas. Indeed, the business lines are collaborating in relation to the early engagement model, Siebel improvements and technical networks. In relation to technical networks, LB&I is starting to increase the emphasis on these networks in building capability across all functional lines. We are allocating SES [the ATO's Senior Executive Staff] sponsors to these networks and ensuring network membership includes staff from Active Compliance and Interpretative Advice areas.

It is important for S&ME (as it is for all BSL) to ensure the capability levels of staff in IA are aligned with the risks and issues being handled in AC areas in order to ensure a smooth transition from AC to Objection. As the Active Compliance program develops and the focus shifts to different or more complex issues, it is critical that the ATO use any cross business line synergies to develop the skills of staff (whether the staff are in IA or AC). There would be clear synergies and benefits for both S&ME and LB&I to explore better use of technical networks. Alignment of capabilities across IA and AC work functions has been a challenge for LB&I, and one way we try to ensure that capability levels are aligned is through the technical networks.<sup>8</sup>

1.33 Whilst the potentially larger quantum of revenue involved may justify the LBI business line's increased access to technical support (compared with the access of SME officers dealing with S4 cases), in the IGT's view, more could be done to improve the support given to SME officers.

## **TRANSFORMING TAX TECHNICAL DECISION MAKING (TTTDM) PROJECT**

1.34 Since 2005, the IGT has raised concerns with the ATO's technical decision making function in a number of IGT reviews, most recently in the IGT's review into the ATO's large business risk review and audit policies, procedures and practices.<sup>9</sup> The IGT is pleased to see that the ATO has heeded those concerns by starting a project to

---

<sup>8</sup> 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, pp. 12-14, 22-23.

<sup>9</sup> Report into the Australian Taxation Office's large business risk review and audit policies, procedures and practices, September 2011, available at [www.igt.gov.au](http://www.igt.gov.au).

improve the tax technical decision making function (the Transforming Tax Technical Decision Making Project or TTTDM project). The ATO advises that this project is aiming to establish and extend early engagement mechanisms (such as those used in the priority rulings process). The current function involves the requirement to escalate class rulings to a Centre of Expertise (COE) or a Tax Counsel Network (TCN) officer whether or not there are precedential issues involved, unless it is a priority ruling (in which case these officers are engaged from the beginning of the process).

1.35 The TTTDM project was undertaken as a result of the recommendations from an ATO internal review called the Law Improvement Project (LIP) review. The LIP focussed on identifying the practical steps that should be implemented to improve the corporate business processes for delivering COE and TCN interpretive advice.

1.36 The ATO advises that this project is in its early stages, is expected to take a number of years to complete and is not expected to affect the SME business line in the short term.

1.37 During the review, the SME business line was involved in a pilot of the TTTDM project. This began in September 2011. The aim of the pilot is:

to ensure that specialist technical resources from areas such as CoEs and TCN are involved in and providing advice and assistance on case work early in the life of a review or audit case. This pilot will include having these specialist staff involved in taxpayer interviews and discussions where necessary.<sup>10</sup>

1.38 In the IGT's view, a number of issues arising from this review provide an opportunity for the SME business line to influence the TTTDM project to deliver needed outcomes on a practical level – for example, as indicated above, guidelines could be developed to clarify the type and level of assistance that technical officers provide to compliance officers.

## **ADDITIONAL GOVERNMENT FUNDING**

1.39 The ATO has received additional funding for other specific compliance initiatives involving larger SMEs, HWIs and WAs. These are discussed below.

### **The ATO's HWI taskforce and Government funding**

1.40 In May 1996, the Government allocated additional funds of \$19.2 million over two years so that the ATO could establish a HWI taskforce to expand the ATO's understanding of tax planning techniques used by HWIs and the resulting compliance risks. Prior to this taskforce, any HWIs were examined by the ATO's small business or large business areas.

1.41 At the end of its first year of operation, the HWI taskforce consisted of 99 FTE staff, identified 254 HWIs and commenced 16 audits.

---

<sup>10</sup> Australian Taxation Office, written communication to the IGT, 23 September 2011.



1.42 The HWI taskforce was initially managed within the LBI business line. The taskforce developed a different approach to compliance that was based on understanding the entire group effectively controlled (as opposed to legally owned) by the HWI. It therefore included all entities in which the HWI had a key decision making role.

1.43 In the 2006–07 Federal Budget, the ATO received \$81.6 million in additional funding to maintain tax compliance amongst HWIs and their associated entities (the HWI Policy funding). This funding covered the four-year period from 2006–07 to 2009–10. At this time, the HWI taskforce was also moved into the SME business line as there was considerable commonality in taxpayer profiles and tax risks between certain HWIs and closely held private SME groups.

1.44 The HWI taskforce's staffing numbers increased from 99 FTE staff in July 2006 to 361 in May 2010. This expansion increased the numbers of reviews and audits undertaken. In 2008–09, 936 reviews of HWIs were undertaken. As at 31 March 2010, 167 HWI audits were underway.

1.45 Liabilities raised by the HWI taskforce in 2008–09 totalled \$530 million compared to just \$31 million in 1997, when the HWI taskforce was first established, and \$166 million in 2006 before the additional funding was made available.

### The Income Tax Investment (ITI)

1.46 As part of Mid-Year Economic and Fiscal Outlook (MYEFO) 2007–08 process of October 2007, the ATO received additional funding of \$446 million from the Government to expand the income tax compliance program over four years from 1 July 2008–09 – the Income Tax Investment (ITI).

1.47 As a result of this government funding, the ATO is expected to deliver an additional \$3.7 billion in revenue over four years. This revenue has 'direct' and 'indirect' components. 'Direct revenue' is revenue collected through enforcement activity. 'Indirect revenue' is said to be the increase in revenue achieved as a result of the combination of initiatives including 'help and education', 'assistance and advice' as well as the broader deterrent effect of the ATO's compliance program.

1.48 Although a revenue return to government is incorporated in this funding, it is not linked to specific ATO activities.

1.49 Under the ATO's internal arrangements, the SME business line was allocated \$53.1 million of this funding over a four-year period. This funding is being used to risk review all SMEs in the S4 market segment.

### The Income Tax Investment Additional Compliance Dividend Component

1.50 In the 2008–09 Federal Budget, the Government provided the ATO with additional funding of \$256.9 million over four years to enhance its compliance activities, particularly for large businesses and HWIs (the ITI Additional Compliance Dividend Component). This measure is expected to deliver an additional \$1.98 billion over four years.



1.51 The SME business line was allocated \$89.2 million of this funding over a four-year period.

1.52 The overall funding associated with the ITI and ITI Additional Compliance Dividend Component totals over \$700 million and is expected to deliver a total of \$5.7 billion in additional revenue. The funding associated with this measure was allocated across the ATO's Compliance, Law and Operations sub-plans.

### Strategic Compliance Initiative

1.53 In the May 2009 Federal Budget, the Government provided the ATO with additional funding of \$302 million over four years to manage taxation compliance risks related to Australia's economic recovery (the Strategic Compliance Initiative).

1.54 The SME business line was allocated \$68.9 million of this funding over a four-period to identify and profile WAs. The ATO advises that this project aims to 'instil community confidence by demonstrating that 'Wealthy Australians' pay their fair share of tax'. Approximately three-fifths of the SME business line's allocated funding for this initiative will be used to fund the MEI business line's workforce assisting with this project.

1.55 The overall additional revenue this initiative is expected to deliver is \$285 million.

1.56 In summary, the SME business line received the following government funding to deliver on the following initiatives.

**Table 1: Government funding of selected ATO initiatives**

	<b>HWI Policy Funding</b>	<b>Income Tax Investment (ITI)</b>	<b>ITI Additional Compliance Dividend</b>	<b>Strategic Compliance Initiative (Wealthy Australians)</b>
<b>Announcement date</b>	May 2006 Federal Budget	MYEFO October 2007	May 2008 Federal Budget	May 2009 Federal Budget
<b>Period covered</b>	2006–07 to 2009–10	2008–09 to 2011–12	2008-09 to 2011–12	2009–10 to 2012–13
<b>ATO Funding received (a)</b>	\$79.5m (Budget papers \$81.6m)	\$487.6m (Budget papers \$446m)	\$277.9m (Budget papers \$256.9m)	\$302.1m (Budget papers same)
<b>SME business line allocation of funding over 4 years</b>	\$62.1m	\$53.1m	\$89.2m	\$68.9m (split with the MEI business line)
<b>FTE staff at final year of investment</b>	180	226	174	171 (5:3 split with the MEI business line)
<b>Deliverables:</b>				
- Direct Revenue	\$770m	\$350m	\$510m	\$285m
- Indirect Revenue	-	\$630m	-	-

Note (a): Discrepancies exist between figures quoted in the Government's budget papers and funding received by the ATO. Budget papers reflect the Government's fiscal balance and excludes items such as superannuation, workers' compensation, revaluation adjustments and depreciation which are included in the ATO's allocated funding.

Source: ATO presentation to IGT staff, 15 May 2010.

## CHAPTER 2 — TECHNICAL CAPABILITY AND SUPPORT

2.1 It is generally acknowledged that to foster community confidence in the ATO's activities in the SME market segment, SME officers need to discharge their duties confidently, expeditiously, equitably and accurately. Such community confidence is critical to voluntary compliance with the taxation laws.

2.2 Overwhelmingly, however, submissions to the review raised the technical capability of SME officers as the main issue of concern. A number of examples were provided of SME officers failing to detect main areas of risk which appeared to be obvious to taxpayers and their advisers. Many submissions also expressed concern that much time and expense was spent in 'training up' SME officers so that the officers could understand sufficient commercial, accounting and tax technical concepts to conduct the compliance activity.

2.3 It should also be noted that submissions also provided examples of capable SME officers who conducted audits professionally, quickly and resolved disagreements fairly and effectively. These examples were, however, provided for the purpose of contrasting the examples of staff with purported lesser capability to deal with complex technical work.

2.4 Compliance work in the S4, HWI and WA areas can involve very complex technical work. Stakeholders have expressed the view that some larger SME cases may be more complex than large business compliance cases. This is because larger SME cases may have similar issues to large business cases as well as other complex matters, such as trust and Division 7A issues or they may not have access to exclusions or carve outs that are available to public company groups.

2.5 During the review, the ATO acknowledged that some SME compliance areas were still building their capability. The ATO advised that further work was underway to improve capability – for example, ATO capability development initiatives, such as the Integrated Capability Development Framework, the learning curriculum, the learning pathway and performance development agreements provide a structure to deliver and develop much needed content for capability development programs.

2.6 The IGT has observed a number of other substantial steps the ATO is taking to improve levels of staff capability such as the SME business line's focus on training and development, assessing the effectiveness of capability development measures and setting the aspirational measure of staff being capable of doing the most complex work (with appropriate support) within 3 years. These are positive moves which should direct the focus of the SME business line towards improving staff capability.

2.7 The IGT believes that improving staff capability as quickly as possible will resolve many of the issues observed in this review. There are lead times required in developing capability and there is a need to maintain that capability once developed.

2.8 The ATO itself recognised that the SME business line will face significant staff capability challenges in the next few years. As such, the ATO has given significant attention to structures that should support the development and maintenance of staff capability, including:

- staff capability development which is intended to have a 'line of sight' with the ATO's business intent;
- a business intent which considers that taxpayers' perceptions of SME staff capability are important;
- a capability development framework and structure which supports SME staff to develop the skills and knowledge that the SME business line expects those staff to possess; and
- monitoring a range of indicators to assess whether the capability development framework was effective in developing staff.

2.9 The IGT considers that the abovementioned ATO work is a positive step and that there is scope to take further steps to improve the overall capability of SME officers, including through retention, training, development, mentoring and the like. These areas are discussed in more detail below.

## **COMPLEXITY OF CASE WORK IN THE S4 MARKET SEGMENT**

2.10 Case work in the S4 market segment involves large businesses that were previously dealt with by the LBI business line. Most of these taxpayers are part of CHPGs that are linked to HWIs. They involve issues as complex as that seen in the HWI area. Another large proportion of these S4 cases involve public companies where the issues encountered may be as technically challenging as any other large case dealt with by the LBI business line, although the materiality of risks is likely to be lower in groups with lower turnover.

2.11 An ATO internal report also observed that work in the HWI market is becoming more complex, having impact on the ATO's compliance activities in these market segments:

... the complexity of the work is clearly shifting, such that S&ME has acknowledged that the high volume and medium complexity work is becoming lower volume and more complex. This is also supported by staff assertions during interviews carried out during this review.

The complexity and intensity of the work program is articulated in the ATO Compliance Program. It would appear that there is a continued focus (albeit with an intensified coverage) of Private Equity Groups, Wealthy Australians, HWI and the \$100-\$250 [S4] Market Segment.

However, the intensity is more than simply increasing coverage and involves a properly considered risk assessment of the patch (through a risk differentiated approach). Accordingly, the issues being identified will necessarily be most likely the higher risks.

... Indeed, the S&ME compliance plan already identifies the increasing emergence of ... complex areas (which are complex from both a factual and legal perspective) ...

This presents the S&ME Executive with a new set of challenges — including how to position it to deal with increasing complexity of work along the compliance pipeline.<sup>11</sup>

2.12 During the IGT's review, submissions from some ATO staff indicated that senior SME business line officers did not believe work in the S4 or HWI market segments was of a particularly complex nature. The ATO internal report considered this issue and observed that:

It was claimed that Senior Managers (at the director level and above) do not appear to appreciate the complexity of the work in IA [the Interpretative Assistance area of the SME business line]. The claims suggest that there is a lack of proper management of the work because they expect staff to process all objections as if they were of equal complexity. This was an issue that was unique to Box Hill site. There was no evidence to suggest that management lacked appreciation of the work complexity. On face value, the complexity of cases is being considered by managers (as illustrated by the way in which planning documents are developed and monitored). However, it is apparent, that the views of managers in relation to the relative complexity of work were not aligned with the views of some staff. Moreover, from discussions with staff, it appeared that some staff felt there was a 'delineation' or 'split' between senior leaders who could provide technical leadership on casework and those who were administrators. Accordingly, the accusation that managers consciously ignored the complexity of case work in their plans cannot be sustained. However, there clearly is a concern that management need to revise their assessment on the complexity of casework under the current environment because cases are becoming increasingly complex.<sup>12</sup>

2.13 In relation to better identifying the complexity of work, during the review the ATO stated that it would take certain action:

... We will design and build a 'complexity measure and indicator' into our case selection process to enable us to better understand the nature of case work we plan to undertake. The indicator will also provide us with a better basis for planning our resource needs and allocation of the correct resources to match the case work. We plan to have this in place for the 2012/13 year.<sup>13</sup>

2.14 In the IGT's view, SME cases may be as complex as LBI cases, if not more so, because similar issues to LBI cases may be encountered as well as other complex technical issues such as those relating to trusts and Division 7A. The ATO is increasing its focus on more complex work in the S4 and HWI market segments while maintaining its focus on higher volume and less complex cases of lower turnover SMEs. Given the comparative difference in capability needed, assessing cases according to their complexity and resourcing them accordingly is critical to the success of the ATO's commitment to Government and affected taxpayers.

---

11 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, pp. 12-13.

12 Ibid, p. 21.

13 Australian Taxation Office, written communication to the IGT, 23 September 2011.

## RECOMMENDATION 2.1

*When selecting SME (including S4, HWI and Wealthy Australian) cases for compliance activity, the ATO should determine the overall complexity for the cases and resource those cases accordingly.*

ATO response: Agree

We will be implementing a case complexity indicator into our case selection processes for review and audit case work.

## STAFF UNDERSTANDING OF THE END-TO-END PROCESS

2.15 ATO officer understanding of the end-to-end process improves awareness of the impact that audit work may have on downstream events in the process (such as objections and litigation). Awareness of these impacts helps ATO officers to make balanced decisions in the best interests of the system as a whole. It is critical to view the compliance plan as a single end-to-end process, rather than separate functions.

2.16 In this respect, an ATO internal report also observed that improved understanding of the roles and responsibilities would address ATO staff concerns with the differing views on the roles of different ATO officers:

The IA and AC areas are committed to building a [sic] better and closer working relationships that will increase the quality of the end to end process and produce efficiencies in the end.

Indeed, S&ME is working closely with LB&I on a number of fronts — including the Early Engagement Model, Siebel systems and technical capability.

However, concerns were often raised about the role of different stakeholders in the end to end process. In particular, there were many differing views on the role of case officers, objection officers, STL [Senior Technical Leadership area of the SME business line — discussed further below] and case leaders in the compliance pipeline. The concept of independence was often raised and there were different views as to whether STL officers or case leaders involved in AC work could also be involved in the objection. The concept of Independence has been thoroughly considered as part of the processes in the Early Engagement Model and also as part of the Dispute Resolution Strategy. Accordingly, any recommendations made in this paper are subject to any finding arising from the above models.

In particular, a fully integrated process map is usually a good guide to assist staff to understand their role within the business model. It would be useful to commence work on developing such a process map.

#### Recommendation 9

Use the SNC [Serious Non-Compliance area of the ATO] template (on end to end process) to develop clear guidelines on the roles and responsibilities of key stakeholders in SME pipeline work and what type of work should take priority.

The concept of independent review and how objection officers should use STL and case leaders in objection work should be clearly spelt out.<sup>14</sup>

2.17 This ATO internal report also observed that guidelines should be developed to improve understanding of the roles and responsibilities of ATO officers involved in SME compliance work:

The document [a draft document spelling out the approach taken by the SME business line to incorporate the principles of 'Early Dispute Resolution' into its work practices and to enhance the interaction between IA and AC staff as part of the end to end process] is presented as Guidelines and therefore provides staff with clear direction on their roles and responsibilities in the end to end process. The guidelines compliment this paper and address many of the concerns raised here in relation to the clarification of the roles of key stakeholders. Accordingly these guidelines should be endorsed and marketed in S&ME. Moreover, consideration should be given to presenting these guidelines in the form of a template ...

#### Recommendation 8

The end to end guidelines paper be developed further and presented in a template format ... that sets out the roles and responsibilities of all stakeholders in the S&ME compliance pipeline – including risk officers, case officers, advice officers, objection officers, STL and case leaders etc<sup>15</sup>

2.18 In accordance with recommendations 8–9 of the ATO internal report, 'Review of interpretative advice as part of the SM&E pipeline', the IGT considers that improved understanding of the roles and responsibilities of different ATO staff involved in compliance activities will go some way to addressing some of the underlying concerns raised by submissions to this review.

### RECOMMENDATION 2.2

*The ATO should improve understanding of the roles, responsibilities and accountabilities of the different staff involved in the end-to-end process of SME cases:*

- a. by ensuring clear guidelines on the roles and responsibilities of key ATO stakeholders in the end-to-end SME case process and the priority associated with them are available; and*

---

<sup>14</sup> 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, pp.28–30.

<sup>15</sup> Ibid, p. 29.

## RECOMMENDATION 2.2 (CONTINUED)

- b. *including in those guidelines, the specific roles, responsibilities and accountabilities of:*
  - i. *SME officers, such as risk officers, case officers, advice officers, objection officers, Senior Technical Leadership officers, case leaders, senior management officers; and*
  - ii. *non-SME officers, such as COE and TCN officers.*

ATO response: Agree

We will review and as necessary update our procedural instructions and documentation to ensure roles and responsibilities of the S&ME officers involved in the end to end case processes are clear.

The current corporate 'Transforming Tax Technical Decision Making' (TTTDM) project will provide clear roles and responsibilities of CoEs and TCN staff.

## LEVEL OF STAFF CAPABILITY

2.19 Many private sector submissions to the IGT commented that, in risk reviews of S4 taxpayers, they observed a lack of technical knowledge and skills (accounting and tax law) and relevant commercial expertise. Some commented that this led to the SME officer missing key technical risks in risk reviews which should have been obvious on the information available. In one extreme example, an S4 taxpayer claims that they paid approximately \$500,000 in fees to their tax adviser during a risk review primarily because of lack of understanding by the SME officer of the taxpayer's business and the technical issues around the business. They say that throughout the course of this risk review, the taxpayer's advisers were required to explain to the SME officer the technical issues across a number of meetings – essentially providing lessons in the accounting and tax treatment of the areas under review.

2.20 The SME business line is also aware of lower level of current staff capability in risk assessments in the S4 market segment. An ATO SME business line draft report entitled, *Segment 4, Risk Scan, Report 2: Risks and Drivers*,<sup>16</sup> identified that officer skills and knowledge are sometimes poor with the impact that some staff are missing significant risks to revenue. The draft report also observed that the support given to compliance officers may not be of the same level as that given to other areas that deal with cases of similar complexity.

---

<sup>16</sup> 'Segment 4, Risk Scan, Report 2: Risks and Drivers', a draft report prepared by the SME business line's Active Compliance Risk and Intelligence area, 26 February 2010.



2.21 In this respect, a recently commissioned ATO internal report also observed that poor quality audits were a common complaint among SME IA officers and that guidelines should be developed to address those complaints:

In many ways, the guidelines cover the issues or risks raised by staff in [another part] of this paper. That is, the guidelines address some of the common complaints in relation [to] poor quality audits;

- ☐ lack of evidence;
- ☐ no statement of facts;
- ☐ poor document management; and
- ☐ lack of properly consider[ed] position – protective assessments due to time constraints and assessment issued while audit still underway.<sup>17</sup>

2.22 The ATO advises the IGT that it relies on its collective capability as no one staff member has all the requisite skills and experience to appropriately deal with all issues that they may encounter. The ATO also advises the IGT that the collective capability is seen as a means to build individual staff capability.

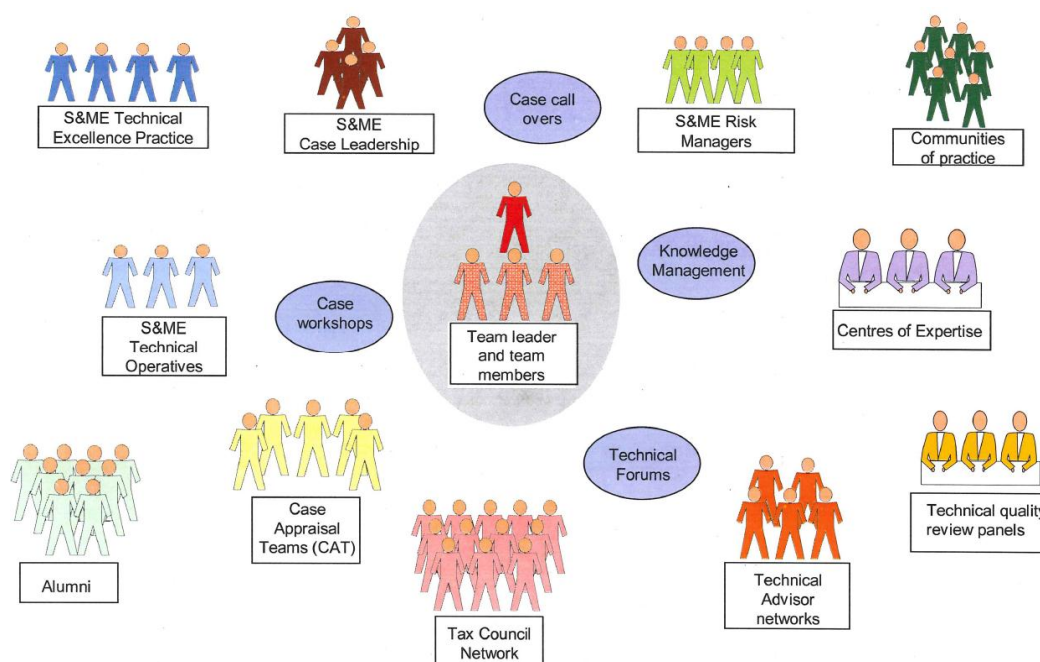
### Collective capability

2.23 The SME business line's model of collective capability is based on the ATO's model and comprises a number of elements. These elements are set out in the figure on the following page.

---

<sup>17</sup> 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, p. 23.

**Figure 2: The SME business line's collective capability**



Source: Australian Taxation Office

2.24 The most significant elements of this collective capability are:

- team leaders/mentors;
- technical excellence (now subsumed into the Senior Technical Leadership area) – a network of approximately 60 Executive Level officers that act as technical specialists and are embedded within compliance teams across the SME business line. Each person also has a number of subject specialities;
- case leadership – 5 Senior Executive Staff that, in addition to assisting case teams with their Active Compliance and Provision of Advice work, also build the technical and case management skills in order to support the organisational development of SME compliance officers; and
- the priority technical issue escalation system and access to the COEs and TCN for the resolution of major, complex issues.

2.25 Submissions raised specific concerns with elements of the collective capability. These are discussed below.

### Team leaders

2.26 The ATO advises the IGT that SME business line team leaders remain accountable and responsible for developing and maintaining the technical capability of their staff. In terms of allocating work, the team leader will also discuss work allocation with the regional directors with the aim of matching the allocated work to the best matched available resources.

2.27 The ATO expresses its expectations of officers' training standards through its internal documentation, such as its Integrated Capability Development Framework learning pathway (this documentation sets out the expected knowledge and skills for compliance officers according to the time spent in the role – discussed further below). However, there is no formal footprint of each officers' skills and experience to facilitate team leaders' allocation of work to officers with the required skills set. This work allocation relies on team leaders' perceptions and their available resources.

2.28 The SME business line also expects team leaders to allocate more experienced officers to mentor other officers.

2.29 However, a SME business line draft report observed that several staff members and managers expressed that it was the first time that they had done certain types of cases, such as large multinational groups, large CHPGs and large investment funds:

Whilst team leaders had concerns, given workloads, they often had little choice but to allocate complex cases to relatively inexperienced staff and provide support as best they could by providing mentoring from more experienced team members (who often had there [sic] own products), and by seeking support from TEP [Technical Excellence Practice, now subsumed into the Senior Technical Leadership area]. Case allocation was further complicated due to cycle times being based on calendar days. Case allocation when there were public holidays or when staff were part time, added additional pressure.<sup>18</sup>

2.30 Additionally, the level of capability in one region may not be of the same level as that in another area, even though they may be tasked to do work of the same complexity, as a recently commissioned ATO internal report observed:

... it is notable that the capability assessment of Box Hill and Sydney IA sites are markedly different even though they are required to undertake similar work. Both areas are responsible for HWI objections and occasionally undertake other matters such as international, trust or CGT issues.

... On the presumption that the capability report accurately reflects the capability levels across the line, consideration needs to be given to the means by which work is allocated to ensure complex work is allocated to teams most capable of performing the work. Alternatively, the capability levels within the teams needs to be supported and enhanced so they can all competently perform complex work.<sup>19</sup>

2.31 Among other things, the ATO internal review urged the assessment of staff capability and the use of that information to manage workflows:

... □ Profiling capability levels of teams and allocating work appropriately – it is important that the capability and experience of IA and Objection teams are properly assessed and that this information is used to manage workflow.

---

18 'Segment 4, Risk Scan, Report 2: Risks and Drivers', a draft report prepared by the SME business line's Active Compliance Risk and Intelligence area, 26 February 2010, pp. 17-18.

19 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, pp. 33-34.

... it is important to recognise that objections that originate from HWI or the \$100 – \$250 million [S4] market will be more complex than other objections.

Accordingly, HWI objections should be allocated to teams who have capable and experienced staff. If teams are made up of new and inexperienced staff, then work should be allocated appropriate to their level of capability.

Currently, it would appear that HWI objections are allocated principally on a site basis. For example, most HWI Objection work is handled in Box Hill or Sydney. This appears to be a historical factor, and something that has been traditionally accepted because of the close proximity of compliance officers and easy access to case files. It is acknowledged that these are important factors in deciding where objections should be handled but they are not the only factors. Consideration must be afforded to the complexity of cases, the capability of staff, the capacity to handle the work, the access to senior technical leadership etc. It is acknowledged that co-location of compliance and objection officers is one of the important factors, but it is not something that is not insurmountable...

It is understood that S&ME has completed capability evaluations of their staff, so it should not be too difficult to assess the capability of teams by site and allocate work accordingly.<sup>20</sup>

2.32 In the IGT's view, there is room to better support team leaders and regional directors in matching case work with the best fit of skills and experience, such as obtaining and maintaining a formal footprint of each officer's skills and experience and allocating work according to that footprint.

### **RECOMMENDATION 2.3**

*To strengthen and better match individual SME business line staff capability for specific cases, the ATO should:*

- a. obtain and maintain a formal footprint of each officer's training and experience to identify gaps when compared to the expected knowledge, skills and experience;*
- b. ensure all SME compliance, interpretative assistance and technical officers have a current learning and development plan that includes skills and knowledge development contributing to the delivery of business outcomes; and*
- c. allocate work to officers according to their footprint and their learning and development plan.*

---

<sup>20</sup> Ibid, pp. 15–19.

ATO response: Agree

With respect to 2.3a our annual S&ME technical capability snapshot process was undertaken in November 2011 with the outcomes expected to be available by around mid December 2011.

With respect to 2.3c we generally allocate work on this basis.

### Senior Technical Leadership

2.33 The Senior Technical Leadership (STL) area was established on 1 July 2010 to provide technical support to all areas of the SME business line other than the Not For Profit area. It was formed by consolidating the technical support areas of HWI and the Technical Excellence Practice who provided support to the General Compliance (GC) area of the SME business line. One of the aims was to provide technical support to case officers when confronted with complexity that they were not in a position to deal with either as an individual or as a team. A key priority for the STL is to build the technical capability of the SME business line by a mix of on-the-job training and preparing and delivering technical resources.

2.34 In late 2010, there were around 65 STL officers comprising of around 53 at the Executive Level 2 (EL2) level and the remaining at lower levels. Over two-thirds of STL officers have over 10 years of ATO experience.

2.35 The STL area has provided a technical specialist directory for SME officers. However, some private sector submissions to the IGT also observed that in some cases the STL officer involved in reviews, although knowledgeable in some areas of the law, did not have the requisite technical expertise in relation to the particular area under review.

2.36 In the IGT's view, the decision to involve any particular STL officer in resolving technical issues in a particular case should be made on the basis of the STL officer's speciality and that speciality's relationship to the issues under review.

### RECOMMENDATION 2.4

*The ATO should involve Senior Technical Leadership (STL) officers in resolving technical issues on the basis of the STL officer's area of speciality or expertise.*

ATO response: Agree

Senior Technical Leadership (STL) staff involved in case work will have the expertise and skill to provide appropriate support to case officers.

STL will continue to be a flexible workforce who can apply their high level technical skills across a range of case work as priorities and workloads require.

2.37 Submissions received from certain ATO staff indicate that the SME business line's collective capability is conceptually sound but relies on the goodwill of technical officers as there is no minimum expectation on the quality and level of support given by them to compliance officers. These staff comment that the express role of STL officers (and the TCN/COEs) is that they are merely advisory and that the compliance officer is the one who must make the decision. They argue that this causes a disconnect between the technical officer and the compliance officer because some technical officers ask inexperienced compliance officers to develop views in a case so that the technical officer can merely check the work, rather than assist them in developing views on the technical issues.

2.38 During the review, the IGT also received submissions from certain ATO staff that were concerned with the technical leadership of managers and directors in the IA area and their interaction with the STL area. A recently commissioned ATO report observed that the underlying issue may relate to accountability and responsibility of technical decision making when issues need to be escalated:

There were concerns raised about the technical competence of managers and directors of the IA team within a structure that has senior technical leaders removed from the functional area and placed in a separate structure (that is, the STL group). Due to the increase in the complexity of work, staff claimed that the managers needed to be technically competent at the EL2 level. However, there was no evidence to suggest that managers or directors were not competent to perform their roles. It is possible that managers and directors may intentionally delegate the technical leadership of cases to the STLs, so the real issue here may relate to accountability and responsibility of technical decision making when issues need to be escalated. In particular, all sites made comments about the STL structure and whether it was optimal to have technical leadership restricted to access to STL. In other words, it was debateable whether technical leadership was something that should be made available to staff only where referral guidelines were met – or whether technical leadership should be available on all complex cases.

... All Directors and Team Leaders in the IA area of S&ME are technical and are selected pursuant to technical criteria. Case officers are encouraged to escalate issues through their Managers and Directors if they need assistance. S&ME also have callovers with the National Directors to review aged and ugly cases. Staff know that they can escalate cases at any time to the National Director level or ask managers to intervene when COE's or TCN are a bit slow. It is understood that this has occurred on numerous occasions. It is also understood that IA staff are encouraged to use the resources provided by STL.

However, the issue appears to be the actual level of technical leadership that can be provided by managers and directors who are primarily responsible for administrative matters. Although it was not explicit in interviews, there were implications that managers and directors were not responsible for technical leadership and the STL officers provide technical advice (as apposed to technical leadership) and the case remained the responsibility of the team. As cases become more complicated, the role of objection officer may also become more demanding and it is likely that the job size would, in many cases, be equivalent to an EL2. Consideration may need to be given to whether the IA function needs to be job sized.

Moreover, when pressed during interviews, there was a general consensus from IA staff that the interaction with STL officers could be better. Staff conceded 'it goes both ways' and they don't readily approach STL. This issue touches on the adequacy of technical leadership in S&ME.<sup>21</sup>

2.39 Whilst, generally, it is not unusual for junior officers to desire more assistance, in these cases, the inexperienced SME compliance officers feel that the technical officer did not guide or mentor them on completing research or determining the relevant evidence needed, resulting in extended delays and missed opportunities. Whether this experience is broader or not, the risk could be minimised by ensuring that compliance and technical staff have shared expectations on the type and level of support to be provided in cases and the specific responsibilities of each party. The SME Executive's June 2010 discussion of case callovers,<sup>22</sup> where isolated instances of friction with technical leaders were raised, also indicate that establishing clear lines of communication and work responsibility would improve the quality of technical support to active compliance cases.

2.40 Relevantly, the SME business line advises that a STL officer is embedded in every AC team. An ATO internal report observed that this placement appears to have contributed to an ATO staff perception that should be addressed:

The perception that STL officers are predominately AC focused and the fact that all STL officers have an AC background is a serious concern that needs to be addressed.

... The STL group report to an Assistant Commissioner who, in turn, reports directly to the ADC (Active Compliance).

Notwithstanding that the management/reporting structure appears to be working effectively, the structure has all STL officers forming part of the Active Compliance line. Prima facie, this creates a misconception that STL's have a principle focus on Active Compliance work. Indeed, this misconception is was manifest in discussions with staff ... Moreover, the SES responsibility or linkages to various corporate capabilities and market segments is incorrectly documented in the S&ME Business Line Plan (Part 2). This inadvertently exacerbates this misconception and needs to be rectified. ...

Staff were not critical of the STL officers – on the contrary, they were very supportive of the STL concept and believed that most STL staff were helpful and accessible. However, the concern with the STL structure was the real perception among staff that STL officers focused predominately on AC work. Staff indicated that they felt reluctant to engage STL officers because they feared the STL would not think they had done enough work on the case to warrant their advice, or that the relevant STL officer was too busy working on other issues. Most sites agreed that it works well if the specific case officer knows the STL personally, or has worked with the STL before.<sup>23</sup>

---

21 Ibid, pp. 22, 28.

22 Minutes of the 30 June 2010 SME Executive meeting, p. 2.

23 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, pp. 22, 32.



2.41 The report also recounted other ATO staff observations of the STL area:

During interviews with IA staff (in relation to the STL group) there were six key themes that arose in the course of the discussion:

By way of summary, the themes relate to;

1. Perception that STL officers were mainly focused on Active Compliance [discussed above]
2. STL officers not proactive in engagement with IA
3. historical factors that need to be overcome
4. 'trade off' leadership and accountability and mentoring
5. the level of comfort staff have in regard to the location of STL across the patch
6. the STL role in managing capability levels.<sup>24</sup>

2.42 In relation to the STL area, the report made a number of recommendations, including:

Recommendation 1

The table at Part Two of the Line Plan is corrected to align the roles of STL and Case leaders to the IA Capability.

Recommendation 10

The STL structure and engagement processes are reviewed and updated if necessary. It may be necessary to market the STL group – by providing an updated communication of their roles, responsibilities and how to engage.

Recommendation 11

STL officers need to be more proactive in their involvement in IA and objection work. One or more of the following recommendations should be considered.

- ☐ Nominate STL officers in IA sites to be allocated directly to IA teams and to provide high level support and direction on technical casework, and / or
- ☐ Amend STL performance agreements to clarify their role in IA and objection, and / or
- ☐ Appoint 'floating STL' who would be available to be used specifically in IA and Objection work as needed.

---

<sup>24</sup> Ibid, pp. 31-33.



## Recommendation 12

STL to be involved in strategy or planning for resources and capability in S&ME (either through committee memberships or exception reports to executive).<sup>25</sup>

2.43 In line with these recommendations of the ATO's internal report, the ATO should ensure that the STL area is more involved in the SME business line's capability development and objection work.

### RECOMMENDATION 2.5

*To improve the Senior Technical Leadership's (STL) contribution to the SME business line's objectives, the ATO should:*

- a. ensure the STL engages with both Active Compliance and Interpretative Assistance officers, in particular objection officers; and*
- b. involve the STL in the SME Executive's planning for resources and capability development.*

ATO response: Agree

STL officers are applying around 25per cent of their total capacity to objection case work.

We currently have 5 STL officers directly allocated to manage a number of High Wealth Individual objections.

### Case leadership

2.44 Since the start of the IGT's review on ATO audits in 2005,<sup>26</sup> the ATO redeployed senior officers to help quickly resolve complex aged cases and model expert case management – Case Leadership. This redeployment was in response to the IGT views that engendering confidence in senior audit staff to make timely and well-reasoned decisions in uncertain situations is an area that can be improved and that, in the more complex cases, early intervention to identify and resolve technical issues by drawing together the right people at the right time to focus on the issues could provide real benefits.

2.45 Some private sector stakeholder submissions to this IGT review observe that Case Leadership's involvement is generally beneficial. However, they believe that their involvement occurs too late in the process to avoid the compliance activity 'going off the rails'.

---

<sup>25</sup> Ibid, pp. 31-33.

<sup>26</sup> Review into the Length of Time to Complete Tax Office Active Compliance Activities, July 2005, Sydney, available at [www.igt.gov.au](http://www.igt.gov.au).

2.46 The ATO is currently examining opportunities to involve its more senior staff earlier in compliance processes – the TTTDM project, as described in chapter 1. The IGT may re-examine the Case Leadership engagement in compliance cases after the TTTDM project has been implemented.

2.47 Some submissions also questioned the nature and involvement of the Case Leadership area. In some cases, they perceived that the area was an underlying reason for the delayed resolution of issues and observed that SME compliance officers appeared unable to progress cases where Case Leadership was intractable. In the IGT's view this indicates that greater clarity is needed in relation to the Case Leadership's role, responsibility and accountability in its involvement with SME cases.

2.48 As discussed in chapter 5, the ATO has agreed to extend the scope of its *Wealthy and wise* booklet to the entire SME market segment. This will provide an opportunity to give greater clarity to the involvement of Case Leadership in SME cases.

## **RECOMMENDATION 2.6**

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), the role, responsibilities and accountability of the Case Leadership area should be clearly explained.*

ATO response: Agree

## **Tax Counsel Network (TCN)**

2.49 The ATO's TCN is not within the SME business line and is responsible for developing the ATO view. Collectively, the TCN represents the ATO's most senior technical officers.

2.50 In relation to SME cases referred to the TCN, the SME business line has identified a number of trends, including TCN capacity and capability concerns by reason of a small number of TCN officers dealing with a large number of highly technical cases:

It was noted that it was often the same Senior Tax Counsel (STC) that were involved in the same types of issues. This raises both a capacity and a capability concern for the ATO.

In terms of capacity, overloading a small number of STC with responsibility for a large number of highly technical cases ... places increased pressure on those STC and reduces the capacity they have to deal with each case. In terms of capability, continually returning to the same STC reduces the opportunity for other Tax Counsel to build their skills and knowledge. There is also the risk that vital experience will be lost when STC leave the ATO if that experience has not been adequately passed on.

Case Leadership is of the view that an opportunity exists for case teams to have wider involvement from a pool of Tax Counsel as opposed to one dedicated person (especially on GAAR matters). This allows new Tax Counsel to gain relevant hands-on experience

with complex issues and allows the business line to access a wider pool of available expertise. It is recommended that access to a wider pool of Tax Counsel be approved and carried out under the guidance of an STC who is able to pass on their experience and knowledge. This arrangement would help to fully develop the STC's of the future.<sup>27</sup>

2.51 In relation to these capacity and capability concerns, the IGT expects that these issues will be considered and addressed in the ATO's TTTDM project.

## THE CHARACTERISTICS OF EXPERT COMPLIANCE OFFICERS

2.52 The SME business line commissioned a researcher, Inside Story, to provide insights into, and guidance on, accelerating the development of expertise in less experienced compliance officers. The research drew from common themes in literature, opinions of experienced ATO officers and observations of a number of expert and less experienced compliance officers. The research examined SME officers' dealings in compliance cases to identify and capture the characteristics of expert officers' thinking, decision making and processes and the difference in these characteristics to those of less experienced officers. In July 2010, Inside Story presented its report, *S&ME Compliance Officer Research*, which identified the characteristics of expert compliance officers in five core areas and created an 'Expertise Assessment Tool' from these areas:

- 1. strategic thinking, including investigative ability, critical thinking and diagnostic ability;
- 2. draws from previous experience, including the application of knowledge of an industry;
- 3. confidence, including being able to maintain momentum on a case when faced with uncertainty;
- 4. productive working relationships, including the ability to seek cooperative solutions and avoid confrontation, and communicate processes and keep taxpayers informed of progress; and
- 5. negotiation skills.<sup>28</sup>

2.53 The full extract of these characteristics is reproduced in appendix 4.

2.54 The researcher made a number of recommendations, including the following:

- Recruitment and selection

Review standard selection criteria for recruitment of compliance officers to confirm key components of expertise are addressed. Draft new criteria to fill gaps

---

27 'Summary note on S&ME Case Leadership Case Callovers', document attached to the agenda for the 30 June 2010 SME Executive meeting.

28 'S&ME Compliance Officer Research', a report commissioned by and prepared for the SME Executive, July 2010.

Integrate new criteria into recruitment questions, skills tests, practical exercises and reference checks

- Learning and development

Strengthen relevant existing learning pathway disciplines which align more closely to the competencies in the Expertise Assessment Tool. For example, Communications and Relationship Management, Commercial Industry and Client Knowledge and Case Management and Work Practice

Develop learning modules to address strategic thinking sub component competencies in Expertise Assessment Tool. Use a staged learning approach appropriate to experience and competency level to fast track development of these skills from the beginning

Develop a new learning module with a basis in Creative Problem Solving techniques to bring together competencies in Strategic Thinking competency. This could form a capstone learning module once a solid grounding from the Strategic Thinking modules has been achieved

A grid analysis can be utilised to plot expertise competencies on axes of 'Extent of expertise gap' and 'Importance of expertise gap to outcomes' to establish an order of priority for the program of works to adapt and develop new learning modules for compliance officers

- On the job training

Provide compliance officers with work placements across 2 or more compliance areas to build a broad range of experience, strategies and approaches that they can draw on. This will help to establish personal networks and supports collaboration across S&ME Active Compliance teams

- Mentoring

... Provide a broad structure for mentoring aligned to competencies in Expertise Assessment Tool

- Expertise Assessment Tool

Utilise the Expertise Assessment Tool to identify development needs across S&ME and within specific teams.

A pilot with a select group of compliance officers is recommended prior to rolling out the Expertise Assessment Tool more broadly within S&ME. This will enable the identification of:

- Motivating factors and potential barriers to use that can be leveraged or mitigated;
- Training needs of managers using the Expertise Assessment Tool;
- Communication priorities for competent use and encouraging adoption; and

- Further refinement if necessary to the components and sub components of the Expertise Assessment Tool based on learnings from the pilot.

- Team environment and communications

Develop a specific KPI for team managers to ensure that they adopt a consistent 'open-door' policy for staff. With the aim of increasing communications between compliance officers and their managers to aid faster development of expertise and their level of performance on compliance work.<sup>29</sup>

2.55 The SME Executive agreed that a 'next steps' document that considered the impact of the recommendations should be drafted.

2.56 In the IGT's view, the findings of the Inside Story research should be used to assist in the recruitment of SME compliance officers, their training, development, assessment and to inform the basis on which work should be allocated to compliance officers.

## **RECOMMENDATION 2.7**

*With the aim of developing highly capable SME compliance officers, the ATO should refine its approaches to recruiting and developing its compliance officers by using the Expertise Assessment Tool developed by Inside Story to:*

- identify development needs across the SME business line;*
- align recruitment and selection criteria with the identified characteristics of 'expert' compliance officers;*
- align learning and development programs more closely with the identified characteristics;*
- improve on-the-job training and mentoring; and*
- measure the capability development of compliance officers.*

### **ATO response: Agree**

We will implement all aspects of the corporate 'Expertise Assessment Tool' framework (the People System Integration Initiative (PSII) which is currently in development.

We continue our ongoing focus on staff capability build both in terms of formal and on the job training.

---

<sup>29</sup> Ibid.

## **SME BUSINESS LINE'S THREE-YEAR CAPABILITY ASPIRATIONAL TARGET**

2.57 On 30 April 2010, the SME Executive supported four aspirational measures. Aspirational measures:

are intended to challenge the [SME business] line in particular ways in order to motivate and drive performance and outcome improvement without specifically stating what has to happen, the approaches to be taken to achieve the measure or who is responsible for achieving the measure.

... Good aspirational measures appear to exhibit a number of common characteristics. They:-

- (1) Operate across more than one area of our business;
- (2) Are easily understood by all affected staff;
- (3) Are directly measurable as an outcome;
- (4) Represent a genuine challenge to achieve that is, they are not easy to achieve;
- (5) Do not duplicate or otherwise replace or conflict with other existing performance measures; and
- (6) Are motivational in their impact and assist to drive improvement in both the business and the client experience.<sup>30</sup>

2.58 Among the four aspirational measures, one is that within three years of moving into the SME business line, staff will be capable (with appropriate support) of doing the most complex work.

2.59 The SME Executive is aware that 'previous quick analysis, both quantitative and qualitative has pointed out that it takes six to seven years to develop a graduate to the level of a departing officer with 15-20 years of ATO service'.<sup>31</sup>

2.60 The IGT believes that improving staff capability quickly will resolve many of the issues observed in this review. It is a positive step to set an aspirational measure of staff being capable of doing the most complex work (with appropriate support) within three years, as this aspiration should direct business focus towards achieving this aim.

## **SPECIALISATION**

2.61 Taxpayers and issues in the SME business line are diverse. Even within the S4 market segment of the SME business line's work, there are a variety of taxpayers. Around 50 per cent of the S4 market segment is part of a CHPG, around 30 per cent are

---

30 'The proposed aspirational measures', document attached to the Minutes of the 30 April 2010 SME Executive meeting.

31 'SME Succession Planning', p.4, document attached to the agenda for the 22 September 2010 SME Executive meeting.

foreign controlled groups, around 15 per cent are public groups, around six per cent are other widely held groups (such as limited partnerships, managed investment schemes, etc.) and around two per cent are non-profit making groups.

2.62 At present, the SME business line's work is a mixture of specialist teams and general compliance (GC) teams. Specialist teams only deal with specific risks (such as Phoenix and Internationals, HWIs and WAs). Whereas GC teams are expected to work on different clients in different segments opening up a much broader range of activity.

2.63 The SME business line is in the process of integrating certain work. Post-integration HWI and WA work will not be dealt with in specialised teams but by 'Active Compliance Integrated' teams. At the team level, work will involve WA, HWI and GC (including S4) work, but work will be allocated by the team leader according to their perception of staff capability.

2.64 The ATO has advised the IGT that:

The upcoming (October 2011) integration of our active compliance workforce's from high wealth individuals (HWI), general compliance and wealthy Australians (WA) will provide us with further opportunities to enhance capability as we will have EL2s leading each of the active compliance teams and a mix of skilled and experienced staff from HWI and general compliance in each team.<sup>32</sup>

2.65 In the IGT's view, whilst officers would benefit from exposure to a wide group of taxpayers and industries, there is merit in some level of specialisation. Such specialisation would allow the officers to be better acquainted with the affairs of taxpayers and industries as well as the issues commonly encountered.

## **RECOMMENDATION 2.8**

*The ATO should facilitate a degree of SME compliance officer specialisation by taxpayer type or industry to better equip them for conducting compliance activities and become better acquainted with the common arrangements of taxpayer types and industries.*

**ATO response: Agree**

Where we see specific risks, issues or business processes in an industry or taxpayer type we will provide compliance officers with additional technical support and/or industry knowledge to ensure they fully understand these matters in the context of the review or audit they are engaged in.

## **NUMBERS OF STAFF TURNOVER**

2.66 Annual turnover of staff in the SME business line has averaged around 20 per cent over the last three years. This is not to say that all staff leaving are the most experienced and all new staff entering have no experience in tax. There are likely to be

---

<sup>32</sup> Australian Taxation Office, written communication to the IGT, 23 September 2011.



a variety of skills sets and experience. However, this turnover of staff does present additional risk to the retention of overall corporate knowledge and experience in relation to the S4 and HWI market segments. This risk is highlighted in the SME business line's 2010 Health of the System Assessment (HOTSA):

□ Recent moves of experienced staff out of S&ME arising from workforce shifts required at the beginning of 2010-11 also represent a significant on-going challenge to our capability. Whilst new staff will join S&ME from other parts of the office including ME&I and LB&I, it needs to be recognised that the skills gap between those leaving and those joining is, in many cases, substantial and will take several years to close.

... What are the key risks to our internal capability?

... □ Workforce shifts — In addition to the above recruitment issues, we are also managing the shift of staff between ME&I, S&ME and LB&I in line with ITI requirements. At the beginning of 2010-11, 44 staff will move from S&ME to LB&I, and we will gain 6 from LB&I and 22 from ME&I. This will result in experienced staff moving out of S&ME and inexperienced staff moving in.

□ Increasing compliance commitments — Related to the above point, there is escalating pressure to balance our formal capability development with increasing compliance commitments associated with HWI, Income Tax Investment and 'Wealthy Australians' projects. Having appropriate numbers of the right staff in place this year will be crucial to meeting our commitments over the next three years.

□ Recruitment and retention of staff — In previous years, we identified risks associated in not being able to attract and retain staff with appropriate skills. While attrition rates have dropped due to the current economic climate, we still have around one third of our workforce over fifty years of age. Where possible, we will seek to recruit externally to attract new expertise by taking advantage of labour shedding in the private sector.<sup>33</sup>

2.67 Annual turnover of roles within the SME business line (that is, including people promoted within the SME business line) averaged higher, at around 27 per cent. The ATO expects that this percentage of turnover of staff will likely persist into the foreseeable future.

2.68 The SME business line is working to understand the staff turnover, from which areas SME staff have left, where they have come from and the impact on workforce management. The following table sets out the detailed figures over the period March 2010 to February 2011.

---

<sup>33</sup> 'S&ME Income Tax HOTSA 2010 - Compliance Sub-plan Health of the System Assessment (HOTSA)', pp. 28-30, document attached to the minutes of the 16 September 2010 Risk Management Committee meeting.



**Table 4: SME staff losses over March 2010 to February 2011**

S&ME Losses - detailing gaining BSL / Plan																
Month	Compliance BSLs									Other Sub Plans					Left ATO (separated)	Total Losses
	ATP	CS&C	EXC	ITX	LB&I	MEI	SNC	SPR	TPALS	OPS	EST	LAW	CS&L	P&P		
Mar-10		1								1				1	3	6
Apr-10	1				1	3						1			3	9
May-10	1		1		3	2				1					2	10
Jun-10		1	1		4	3	1	1	1	3		1			4	20
Jul-10				1	1	4		2	10	1	1		14		8	42
Aug-10		2			13	2	1		7	3	2		1		2	33
Sep-10	3			2	15	2	3		3	2			2		2	34
Oct-10				4	9	3	2		4	2					7	31
Nov-10	1			2	4	4	2		5	4	2				6	30
Dec-10	1			7	12	1	1	1	4	2	1		3		3	36
Jan-11	2	1		2	5	2		3	1	2			2		10	30
Feb-11	2	2		3	4	2	1		1	2	2		1		3	23
<b>Totals</b>	11	7	2	21	71	28	11	7	36	23	8	2	23	1	53	304
<b>Percentage</b>	3.62%	2.30%	0.66%	6.91%	23.36%	9.21%	3.62%	2.30%	11.84%	7.57%	2.63%	0.66%	7.57%	0.33%	17.43%	100.00%

Source: Australian Taxation Office

**Table 5: SME staff gains over March 2010 to February 2011**

S&ME Gains - detailing losing BSL / Plan																
Month	Compliance BSLs									Other Sub Plans					Sourced externally (recruitment)	Total Gains
	ATP	CS&C	ITX	GST	LB&I	MEI	SNC	SPR	TPALS	OPS	EST	LAW	CS&L	P&P		
Mar-10	2					16			1	1					2	22
Apr-10					3	3	1	1	2					1		11
May-10	1				1	1				1		1				5
Jun-10	1				1	3				7	2	1				15
Jul-10	2	1			2	12		1	1	4				1		24
Aug-10			4		7	18	2	1		5	1			12	9	59
Sep-10			2		1	1	3			5				2	1	15
Oct-10	3		5		1	3	1			2	3				2	20
Nov-10			2		3	2	1	2		10						20
Dec-10			2		1	4	2	1	3	2	1			3		19
Jan-11	4		4		4	3	2	3		2	1			23	9	55
Feb-11			2		1	6				3					2	14
<b>Totals</b>	13	1	21	0	25	72	12	9	7	42	8	2	0	42	25	279
<b>Percentage</b>	4.66%	0.36%	7.53%	0.00%	8.96%	25.81%	4.30%	3.23%	2.51%	15.05%	2.87%	0.72%	0.00%	15.05%	8.96%	100.00%

Source: Australian Taxation Office

2.69 In terms of the 'churn' of staff, the ATO considers that the SME business line is the 'feeder group' for other areas of the ATO, such as the LBI business line and that this 'churn' is part of the design of the ITI by having a 'pull through' of resources from the MEI business line, through the SME business line to the LBI business line. The ATO also considers that the churn comprises of staff of differing capability – that is, it is not only experienced staff leaving and only inexperienced staff entering the SME line.

2.70 On 30 April 2010, the SME Executive were made aware that the LBI business line were looking for approximately 70-109 FTE staff from the SME business line (including 46 EL2s and 1s) by 1 July 2010 to work on the Strategic Compliance Initiative. The LBI business line requested staff with expertise in specific areas, such as transfer pricing, CGT, losses, etc. There were also a number of MEI business line staff that were to be transferred to the SME business line.

2.71 Comments from some SME officers have suggested that the LBI business line has recruited many experienced SME officers to replace their retiring staff – a trend that they expect to continue for at least two years.

2.72 Of the SME business line's areas, Interpretative Assistance, Active Compliance and Risk & Intelligence, around one-third (439 of 1299) were over 50 years old, and just over half (696 of 1299) were over 45 years old. At the 18 November 2010 SME Executive meeting, the SME Executive stated that there were 'some significant future workforce planning issues around age demographics that SME needs to address'.

2.73 The IGT observed that there is a general perception that the LBI business line employs more capable staff than the SME business line because of the greater quantum of revenue involved. In the IGT's view, it is an important aim to ensure that more capable staff deal with areas of higher risk and consequence. However, a balance should be struck between this aim and ensuring that the SME business line retains enough of its workforce capability to perform its function effectively. The ATO should carefully consider whether the LBI business line could use more staff from business lines other than SME. Additionally, it should also consider whether the SME business line could use more capable staff from other areas, including the LBI business line, COE and TCN.

## **RECOMMENDATION 2.9**

*In balancing the need for more capable staff to deal with areas of higher risk and consequence with the need of the SME business line to retain enough of its workforce capability, the ATO should ensure that:*

- a. the LBI business line recruits staff from all business lines including the SME business line; and*
- b. the SME business line recruits capable staff from all areas including the LBI business line, COE and TCN.*

**ATO response: Agree**

**Our current corporate recruitment process facilitates this approach to recruitment for both internal and external recruitment.**

2.74 There are no exit interviews with staff moving to other areas of the ATO, but the SME business line assumes the main reasons for staff leaving the SME business line is promotion or retirement.

2.75 In the IGT's view, it is important to conduct exit interviews for staff moving to other areas of the ATO irrespective of the reason why a staff member is leaving from the SME business line. These departures are a good opportunity to gather information which could assist it in improving staff retention.

### **RECOMMENDATION 2.10**

*The SME business line should conduct exit interviews for staff leaving to other areas of the ATO irrespective of the reason why a staff member is moving.*

**ATO response: Agree**

We will re invigorate the process of undertaking exit interviews of staff leaving S&ME to other business lines. Participation by staff will be voluntary.

### **STAFF ENGAGEMENT**

2.76 On the basis of the ATO's November 2009 staff engagement survey, it is unlikely that the level of staff engagement plays a substantial role in the level of staff churn. The survey concludes that SME staff engagement is high at 82 per cent. Overall, this is higher than other areas in the ATO, the public sector and other Australian based peers. It observed that the SME business line's key strengths were pay & performance management, immediate managers, and values (on par with the norm). The identified areas for significant opportunities were efficiency, training & career development, senior leadership and image.

2.77 These surveys provide an overall picture on Staff engagement. However, during the review the IGT received submissions from a number of current and previous SME AC and IA officers. These submissions indicated dissatisfaction with aspects of the SME business line and, in some cases, were the purported reason for leaving the area.

2.78 The ATO recently commissioned an internal report which included consideration of selected IA teams' views on their engagement with the SME business line. It observed that many issues have been raised by other parts of the SME business line before but remain unresolved:

Notably, many of the issues (but not all) were identified in the 3-1 Leadership Workshops conducted in September and October 2010. ... However, it would appear that many of these issues ... remain unresolved notwithstanding the specific action plans that were agreed to address them. Some action plans may have progressed but it was not communicated for the purposes of this review.

The issues raised during these interviews are summarised below [that is, Resourcing; Complexity of work acknowledged by senior managers; Technical competence of

Managers; STL technical leadership; Capability of staff; Quality of audits; Roles and responsibilities and independent review; Location of objection work].<sup>34</sup>

2.79 In the IGT's view, the ATO could improve its staff engagement in seeking to understand and appropriately respond to their concerns.

## **RECOMMENDATION 2.11**

*To address SME staff concerns in relation to their work, sufficiently senior ATO staff, who are not the subject of the concerns, should:*

- a. conduct open and frank consultation with the relevant staff;*
- b. seek to understand the concerns and their underlying causes;*
- c. communicate consideration of those concerns including what action will be taken; and*
- d. periodically communicate the status of the remedial action.*

**ATO response: Agree**

We require our managers to deal with staff concerns about their work as a routine part of their leadership role.

Where the manager is the subject of the concern we allocate another suitable officer to deal with the matter.

## **RECRUITMENT — PERCEPTIONS OF SME BUSINESS LINE POSITIONS**

2.80 The 2010 SME business line's HOTSA details that 'recruitment is continually problematic for the line'. At the 22 September 2010 SME Executive meeting, it was agreed that the SME business line needed 'strategies to actively recruit new staff to the line, such as line workforce planning'.

2.81 Discussion with staff provides some insight into staff's perceptions of the recruitment processes. At the senior executive site visits in the ATO's National Office in September 2010, one of the concerns raised was in relation to recruitment, particularly the length of time to fill positions, that those performing higher duties may be disadvantaged in future recruitment processes, the length of time spent in higher duties and mechanisms to support mobility. At the Parramatta September 2010 site visit, although generally positive in nature, some comments were received about the perceived anomalous nature of recruitment processes (for example, 'not suitable for an

---

<sup>34</sup> 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, p. 20.

APS 5 but judged suitable for an APS6 role') and lack of development opportunities (particularly compliance work) for call centre staff.

2.82 In the IGT's view, more could be done to understand perceptions of the positions in the SME business line and the recruitment processes. The SME business line should take action to address those concerns to make the SME business line a more attractive choice for potential applicants.

## **RECOMMENDATION 2.12**

*In the SME business line recruitment processes, the ATO should emphasise the attractive aspects of the work of this business line such as its complexity, variety and development opportunities.*

**ATO response: Disagree**

We do not see the need to implement this recommendation with respect to recruitment in S&ME.

We remain committed to the current compliance recruitment processes and are of the view that it provides S&ME with the same number and quality of staff as it does for other compliance business lines.

The bulk of the new recruitment into S&ME is through the broader compliance sub plan recruitment program. This program seeks to attract internal and external applicants who have strong tax technical skills and who can adapt to technical work in various parts of the compliance sub plan.

To the extent that we may have any specific SM&E recruitment processes for any specialist positions in the future, we will highlight the attractiveness of the work.

## **STAFF RETENTION STRATEGIES**

2.83 At the 19 January 2011 SME Executive meeting, a 'talent management' strategy document was circulated and it was agreed to send the proposal for further work in the SME business line's Business Operations & Integration Business Management Committee. The strategy aimed at retaining and developing talent as an interim measure pending the roll out over the next 2-3 years of the ATO's corporate strategy. The SME business line strategy document noted that the SME business line has not undertaken actual work to identify people demonstrating high performance and high aspirations. The strategy will be based on the ATO's Indirect Tax area's recent pilot.

2.84 Also relevant is the career and development path within the SME business line. A significant driver for the recent expansion of campaign teams is to assist in recruitment and development of staff. It offers higher volume but lower complexity compliance work, with teams intended to be regularly exposed to new aspects of tax compliance and develop their client interaction and project management skills. It is said to offer a good entry point into compliance work for those staff that are new to the



ATO. This work, however, is mainly targeted at the lower end of the SME market segment. The existing campaign team was recruited from the SME call centre and had relevant skills and knowledge.

2.85 In the IGT's view, more could be done to retain staff, such as establishing a clearer career pathway for existing staff to progress along and deal with more complex work.

### **RECOMMENDATION 2.13**

*The SME business line should take action to retain staff, including establishing a clearer career pathway for existing staff to progress along and deal with more complex work.*

ATO response: Agree

S&ME will manage our staff levels and capability in line with the broader strategic priorities and focus areas of the ATO and the Compliance sub plan.

A clearer career pathway is now available to staff following our recent move to an integrated active compliance workforce where opportunity to undertake a broader range of case work will be available within teams.

## **STAFF TRAINING AND CAPABILITY DEVELOPMENT**

### **The Integrated Capability Development Framework**

2.86 In 2009, the ATO designed and implemented an Integrated Capability Development Framework for delivering training and development to SME officers. The framework aims, amongst other things, to help officers build their professional capability as a compliance officer. It also aims to align staff learning and development with corporate outcomes and that the training curriculum supports the development of skills and knowledge that the ATO expects of officers according to the time spent in the role.

2.87 Team leaders and managers are responsible to ensure that the learning and development plans, as part of officers' performance development agreements (PDA), are in place and include plans to acquire skills and knowledge that would improve the officer's contribution to delivering business outcomes. The skills and knowledge is assessed by reference to the learning curriculum, which comprises a large amount of tax technical and accounting training.

2.88 As at May 2010, the SME business line reported that 92 per cent of all SME officers had a PDA in place. As at November 2010, 99.3 per cent of SME's technical staff had a learning and development plan in place.

2.89 In the IGT's view, the Integrated Capability Development Framework, the learning curriculum and pathway and PDAs provide a structure to develop and deliver much needed content for capability development programs.

### Content of training and development on commercial issues

2.90 The content of the learning curriculum comprises of a significant number of tax technical topics. The Learning Handbook for compliance officers sets out the different topics offered in the Compliance sub-plan's curriculum, this comprises:

- 31 modules in the audit and accounting discipline;
- 64 modules in the case management and work practice discipline;
- 27 modules in the communication and relationship management discipline;
- 21 modules in the corporate discipline;
- 70 modules in the leadership and management discipline;
- 17 modules in the risk and intelligence discipline;
- 52 modules in the systems discipline;
- 272 modules in the tax technical discipline; and
- 12 modules in the client knowledge, commercial and industry focus disciplines.

2.91 The numbers of modules that appear to deal with the commercial or business environment (that is, more than merely outlining legal requirements of particular structures or regulatory requirements defining the entity) affecting taxpayers is comparatively less than the number of tax technical modules to a significant extent.

2.92 In its 2010 HOTSA, the SME business line provided an overview of how it equips its staff with the capabilities needed:

□ We are equipping staff with the capabilities they need but recognise that comprehensive skilling takes time. We are committed to developing the skills and confidence of our staff. We have implemented an Integrated Capability Development System including two externally recognised courses (the Vocational Graduate Certificate and Vocational Graduate Diploma of Taxation Compliance) to incrementally develop capability in technical and leadership skills.

□ We have also implemented the S&ME Compliance Officer Research project to provide a framework to develop the skills of less experienced compliance officers as quickly as possible. This project will inform people management strategies in S&ME, including recruitment, selection, induction, learning and development.

□ Structured learning pathways are currently available in our Active Compliance, Interpretive Assistance and Risk and Intelligence capabilities. All 14 modules of our



Complex Compliance Curriculum have been rolled out with 490 staff attending 54 events across 14 sites.

... □ A recommendation from a report from the HWI case call-over process suggested that staff need more awareness of behavioural drivers as well as a technical understanding of risks. This is particularly relevant as we make the shift to 'Private Wealth' approaches across the line.

□ Several learning products have been developed to support our shift to private wealth, including a foundation level product focussing on complex business structures and an intermediate product focussing on behaviours of Wealthy Australians. These products have been delivered to our initial Wealthy Australians teams in 2009/10 and are planned for further roll out across the S&ME workforce in 2010-11.<sup>35</sup>

2.93 The SME business line determines the needed skills and knowledge through its business management committee. Prior to February 2011, information about training needs had been obtained from managers and then collated into spreadsheets. In February 2011, the SME business line adopted a different approach by engaging in conversations with the SME business line's business leaders to identify business priorities.

2.94 The SME business line also stated that it uses external trainers, such as Certified Practicing Accountants, to provide staff with broader commercial understanding. In 2010, the SME business line stated that it spent around \$1 million on external training providers. The Learning and Development area of the SME business line indicates that heavy reliance on external presenters to deliver this material is not a long term strategy and that in the long term such presentations will be required to be delivered by in-house presenters.

2.95 In the IGT's view, there appears to be little systematic external input into identifying areas for training or in developing training packages, and more could be done in this area. Drawing on Inside Story's research and recommendations (outlined above), training modules that are more specific to particular industries and taxpayer types may be developed, drawing on senior expertise (including observations by relevant Senior Tax Counsel, executive ATO management and external experts) and provide a more thorough understanding of the business environment and related decision-making in particular taxpayer or industry groups that are the subject of compliance action.

---

<sup>35</sup> 'S&ME Income Tax HOTSA 2010 — Compliance Sub-plan Health of the System Assessment (HOTSA)', pp. 28-29, document attached to the minutes of the 16 September 2010 Risk Management Committee meeting.

## RECOMMENDATION 2.14

*With the aim of improving SME business line understanding of commercial and business issues, the ATO should:*

- a. develop programs that provide SME officers with a strong understanding of the business environment and related decision making in taxpayer or industry groups that are the subject of compliance action – such programs should be developed by drawing on:
  - i. input from key tax professional and industry stakeholders;*
  - ii. expertise of Senior Tax Counsel personnel, ATO executive management and external experts;*
  - iii. complaints relating to potential shortfalls in officer training or capability; and**
- b. ensure that before SME officers review/audit taxpayers within a particular industry these officers should have completed, or be accompanied by an officer who has completed, the relevant program of the type outlined in 'a.' above.*

**ATO response: Agree**

Depending on the issue a 'program' might include research, additional support from a specialist officer or additional training.

### Delivery of staff training and development

2.96 The SME business line advises that it has delivered about 2482 hours of training to its staff over the last 21 months through 378 training sessions involving 8350 attendances (staff have attended multiple training sessions).

2.97 At the 16 February 2011 SME Executive meeting, the Executive asked for an initial picture of capability gaps based on learning summaries by workforce and matched against the training that the Learning & Development area indicated that it would deliver. There is no formal footprint which assesses a compliance officer's completed training against those skills that are expected of them according to the three-year learning pathway (discussed above).

2.98 At the May 2010 Newcastle SME senior executive site visit, positive comments were received from SME officers. It was suggested that 'technical capability can be built through training but staff need to acquire a higher level of confidence in dealing

with tax agents and more experienced representatives. Not just training but practical application needs consideration as well'.<sup>36</sup>

2.99 In March and April 2010, the SME business line conducted feedback sessions with its officers, with 85–90 per cent of staff attending. Among the comments that were 'consistently raised across various sites and sessions', SME officers commented that:

- Need further advanced technical training. Lots of foundation training available, but a lack of advanced. Maybe produce some internal DVDs using internal experts to talk about specific issues and risks.
- It can be difficult to manage L&D [the Learning and Development area of the SME business line] activities against case targets.
- Frequency and timing of L&D in some sites is an issue (particularly regional sites).
- Suggestion that a 'resource library' of training be developed over time to provide 'just in time' training and ability to refresh and update on specific topics. This could be DVDs of training delivered live in another site and pod casts (as per the delivery of many uni courses these days).
- Use more technology to support delivery of packages via net meetings, video conferences etc.<sup>37</sup>

2.100 In the IGT's view, the SME business line should consider a broader range of ways to deliver training so that officers have access to information when needed, including a resource library training suite. In relation to the external training already provided, it does not seem to have been captured in a way that allows it to be disseminated more broadly than those who did not attend, or to be reviewed by those that did attend. The SME business line should also consider engaging tax practitioners, academics, business and client management experts to deliver training.

## **RECOMMENDATION 2.15**

*In seeking to improve SME business line staff training, the ATO should:*

- a. provide a broader range of ways to deliver training so that officers have access to information when needed, including a resource library training suite;*
- b. in relation to the external training provided, capture that training in a way that allows it to be disseminated more broadly than those who did not attend and to be reviewed by those that did attend; and*

---

36 'Supportive Site Visit report', p. 7, document attached to the minutes of the 25 August 2010 SME Executive meeting.

37 'Feedback from SME Information Sessions March/April 2010', p. 1, document attached to the agenda for the 12 May 2010 SME Executive meeting.

## RECOMMENDATION 2.15 (CONTINUED)

- c. *engage tax practitioners, academics, and business and client management experts to deliver training on a regular basis.*

ATO response: Agree

S&ME will ensure our training activities make use of the broad range of methods of delivery in line with the current ATO work looking at expanding the methods of delivery of training and development.

We will also make use of externals to develop and deliver training in line with the ATOs Tertiary Education Initiative (TER).

### Capability development effectiveness measures

2.101 Since November 2010, the SME business line has determined and assessed the effectiveness of its capability development measures through a range of indicators, outlined below:

1. upward shift in staff and team leader confidence;
2. build capability to deliver training in a sustainable way;
3. measurement of skilling delivery against plan;
4. learning pathways available to all staff;
5. deliver on commitments;
6. meet/exceed IQF [Integrated Quality Framework] results;
7. contribute to improved cycle times;
8. attract new work to the line;
9. increased staff retention rates;
10. improved strike rates; and
11. improved productivity (quality, cost and through put).<sup>38</sup>

2.102 The SME business line has advised IGT staff that it intends to continue measuring these performance indicators on a six-monthly basis.

---

<sup>38</sup> 'S&ME Integrated Capability Development — performance indicators', 29 November 2010, pp. 5-6.

## RECOMMENDATION 2.16

*The ATO should continue measuring the performance indicators for the effectiveness of its training and development activities.*

### ATO response: Agree

2.103 Of these performance indicators, none appear to consider taxpayer or adviser views on ATO officer conduct or knowledge.

2.104 Credible compliance (which is seen by the SME business line as an essential pre-requisite to achieving the ATO's business intent) exists if 'taxpayers perceive [that the ATO] can identify risk cases and have the resources, including people with the necessary skills, to address those cases'.<sup>39</sup>

2.105 In the IGT's view, routine and systematic capture of external views on staff capability should be obtained as a capability development effectiveness measure. Taxpayers and their advisers are best placed to test whether SME officers have used in their work the needed training and skills.

2.106 The SME business line obtains a measure of external satisfaction with its performances through the Staff Professionalism Survey and Client Feedback Questionnaires. The results of the Staff Professionalism Survey show that the criteria 'sufficient understanding of issue' and 'understood needs' as having the worst performance and having the highest impact on externals' perceptions of ATO staff professionalism. Only a small number of taxpayers respond to the Client Feedback Questionnaires and no non-bias response testing is carried out.

2.107 In the IGT's view, the Staff Professionalism Survey and small response rate for Client Feedback Questionnaires indicate that the SME business line could take more proactive measures to obtain externals' perceptions of SME officers' capability (such as conducting key client visits) and more could be done to understand those perceptions.

## RECOMMENDATION 2.17

*With the aim of improving the assessment of staff capability development effectiveness measures, the ATO should:*

- a. *routinely and systematically capture external views on staff capability as a factor in assessing capability development effectiveness measures;*

---

<sup>39</sup> SME Aspirations Statement 2010-11; Note: Submissions also strongly indicated that ATO staff completing work in such a way on a timely basis was a significant factor in establishing 'credible compliance'.

## RECOMMENDATION 2.17 (CONTINUED)

- b. *take more proactive measures (other than the Staff Professionalism Survey and Client Feedback Questionnaires) to obtain and understand external stakeholders' perceptions of SME officers' capability (such as conducting key client visits); and*
- c. *work with private sector stakeholders to improve SME officers' ability to understand their needs and demonstrate sufficient understanding of the relevant issues.*

ATO response: Agree





## CHAPTER 3 — COMPLIANCE DECISION-MAKING

3.1 Submissions to the review expressed concern with the quality of initial compliance decisions (that is, those in risk reviews and audits) by SME officers and the time and effort needed to raise the issues to a sufficient level within the ATO for appropriate review and resolution.

3.2 It should be noted that the IGT has previously examined compliance decision-making in a number of reviews and recommended action be taken to improve initial compliance decisions.<sup>40</sup>

3.3 The SME business line, itself, has a number of technical panels designed to improve and test compliance officers' decisions making. The SME business line also incorporates control points in the process to review compliance officers' work before decisions to amend liabilities are made, including:

- the team leader and embedded STL officer may review and approve of decisions;
- the National Case Assessment Team (NCAT) approves any case for audit action;
- the Technical Excellence panel reviews large cases, cases involving complex technical issues, and any decision to levy more than \$1 million in penalties;
- SME Case Leadership, COE and/or TCN may be involved in more complex cases; and
- Part IVA decisions are referred to the General Anti-Avoidance Rule Panel for review.

3.4 Substantial recent measures have also been undertaken by the SME business line to improve the quality of its initial compliance decisions. However, there is scope for further improvement in relation to engagement between the active compliance (AC) and interpretative assistance (IA) areas of the SME business line. Other areas for improvement also include, using the Facts and Evidence Worksheet as a means to formulate and develop technical positions, better understanding the reasons why some initial compliance decisions are not upheld on review, resourcing in the IA areas, improving processes involving suggestions of evasion by SME officers and improving the Integrated Quality Framework (IQF) review of SME compliance work. These areas are discussed in more detail below.

---

<sup>40</sup> For example, Review into Aspects of the Tax Office's Settlement of Active Compliance Activities, December 2009, Sydney, available at [www.igt.gov.au](http://www.igt.gov.au).

## RISK IDENTIFICATION AND CASE SELECTION

3.5 Optimal risk identification and case selection are essential to assure the community that revenue collection is appropriately conducted and the compliance burden for taxpayers is minimised and proportionate to identified risks.

3.6 At the broadest level, the ATO's compliance program identifies priority risks to the tax system for potential review. Population segments may be categorised in different ways, such as according to risk, taxpayer type or other factors. The ATO risk rating 'engine' identifies a pool of potential cases for compliance activities according to the business rules for that engine. Compliance officers are then allocated a review case from this pool and seek to address the risk or risks identified and prioritise required action. If after a review the risk is identified as requiring audit, the NCAT reviews such cases and will decide whether to approve the case for audit or not.

3.7 The IGT is of the view that where ATO compliance teams identify what they consider to be further potential risks in the carriage of their (already NCAT-approved) work, a senior officer with the appropriate skill and capability must subject the issue to an appropriate internal approval process before audit teams commit resources to investigative action. Stakeholders have made representation to the IGT that this process is not working as well as it should, giving rise to unnecessary compliance burdens for taxpayers.

### RECOMMENDATION 3.1

*If the ATO wishes to expand the scope of a compliance activity to encompass issues that were not identified at the point of case selection, then it should only do so after subjecting the issues to an appropriate approval process such as business case approval or risk review. This is designed to ensure that the compliance activity is warranted and that overall compliance costs are minimised.*

#### ATO response: Agree

We will reinforce our current process which is that the case officer will discuss the proposed change in scope with their EL2.1 team leader and agree on an outcome which will be documented via case notes in Siebel and communicated to the taxpayer.

3.8 The SME business line also has a stated aspirational strike rate target of 80 per cent for its cases. SME business line analysis in 2010 revealed that the audit strike rate has improved significantly over the 30 months between July 2007 and December 2009 from 54 per cent to around 70 per cent. However, the improvement appears to have reached a plateau at approximately 70 per cent. This suggests that to reach the 80 per cent target current approaches may have run their course and new ideas need to be considered.

3.9 The IGT notes that care should be taken with setting aspirational measures as they can sometimes drive behaviours that cause problems in other areas or merely shift the problem to another part of the process — see for example, the IGT's discussion of

the two-year timeframe for large business audits in the IGT's Large Business Audit and Risk Review report.<sup>41</sup>

3.10 The ANAO is currently conducting a review of the ATO's management of compliance in the SME market with particular focus, among others, on business risk profiling, including an examination of the techniques used to identify and narrow the risk pool, manage risks and select cases.

3.11 The IGT, in the context of this review, is only addressing risk identification from the point of case selection. The IGT has previously raised the ATO's risk differentiation framework and related risk processes as a potential review topic.<sup>42</sup>

## LEVEL OF DISPUTATION

3.12 The level of disputation arising from active compliance activities can be due to a number of factors. This may include a taxpayer's confidence in their position, financial capacity and confidence in the ATO's review or objection processes, to name a few.

3.13 Over the last four years the HWI taskforce has raised over \$1.5 billion in tax liabilities. Approximately 15 per cent of that amount was not disputed. Over half remains in dispute.

**Table 6: Total liabilities raised by the HWI taskforce during 1 July 2006 — 30 June 2010 according to whether settled, disputed or not disputed**

	\$	\$
<b>Total Liabilities Raised</b>		<b>1,513,140,508</b>
<b>Settled</b>		
Collected under Settlement Arrangement	416,808,501	
Reversed due to Settlement	<u>59,479,655</u>	476,288,156
<b>Disputed</b>		
Collected - In Dispute	40,192,467	
Uncollected in Dispute	652,678,174	
Reversed on dispute	<u>110,784,129</u>	803,654,770
<b>Not Disputed</b>		
Collected - Not in Dispute	138,626,845	
Uncollected - Not in Dispute	<u>93,847,916</u>	232,474,761
<b>Penalty Remissions</b>		722,821
<b>Total</b>		<b>1,513,140,508</b>

Source: ATO communication with IGT, 26 March 2011

41 Report into the Australian Taxation Office's large business risk review and audit policies, procedures and practices, May 2011, Sydney, available at [www.igt.gov.au](http://www.igt.gov.au).

42 Ibid.

**Table 7: Total liabilities raised by the HWI taskforce during 1 July 2006 — 30 June 2010 according to whether collected, uncollected or reversed.**

	\$	\$
<b>Total Liabilities Raised</b>		<b>1,513,140,508</b>
<b>Collected</b>		
Collected under Settlement Arrangement	416,808,501	
Collected - Not in Dispute	138,626,845	
Collected - In Dispute	<u>40,192,467</u>	595,627,813
<b>Uncollected</b>		
Uncollected in Dispute	652,678,174	
Uncollected - Not in Dispute	<u>93,847,916</u>	746,526,090
<b>Reversed</b>		
Penalty Remissions	722,821	
Reversed due to Settlement	59,479,655	
Reversed on dispute	<u>110,784,129</u>	170,986,605
<b>Total</b>		<b>1,513,140,508</b>

Source: ATO communication with IGT, 26 March 2011

3.14 In the above tables, the finalised cases amount to over \$820 million in raised tax liabilities. Of those finalised cases, over 20 per cent of amounts were reversed in remissions, settlement or dispute.

3.15 The level of disputation in HWI amendment cases over the last 4 years averages 85 per cent. ATO research shows that liabilities raised in HWI compliance cases were reduced 30 per cent in objection and that 40 per cent of taxpayer objections are upheld fully or in part. The S4 risk review project is in the fourth year of risk reviews, so the development of S4 taxpayer audits and disputes have not matured at this stage.

3.16 Across all of SME and as at May 2011, the SME business line was tracking at approximately 42 per cent of the ATO position being upheld in objections. The SME business line identified:

a need to work more closely with IA and look to identify where we can improve our evidence to support our technical decisions.<sup>43</sup>

---

<sup>43</sup> Minutes of the 17 May 2011 the SME business line's Active Compliance Business Management Committee meeting, p. 6.

3.17 Selected IA teams gave some views in a recently commissioned ATO report. Amongst other things, it observed ATO officer's impressions that there was room to improve the quality of upstream compliance work:

Some audits are reaching objection in a poor state. The most common complaints are:

- ☐ lack of evidence;
- ☐ no statement of facts;
- ☐ poor document management; and
- ☐ lack of properly consider position – protective assessments due to time constraints and assessment issued while audit still underway

These audit practices place undue pressures on the objection phase and require the objection officer to effectively conduct the 'audit'. This problem is further exacerbated because IA officers do not appear to make the best use of STL officers and case leaders. This problem is directly linked to the next point.

There were a number of anecdotal references from stakeholders to the S&ME program that indicated the quality of audits in some areas of S&ME needed to be significantly improved. The general consensus was that complex audits were generally done well but some of the medium and low end work was 'scrappy'.<sup>44</sup>

3.18 During the review the ATO advised the IGT that:

We will be taking part in the upcoming Compliance sub plan dispute review processes and will implement any recommendations relevant to S&ME active compliance work which flow from that review.

We are currently working on an improved reporting interface with the Interpretative Assistance area. This will ensure we can track audit cases which proceed to an objection and thereby undertake ongoing analysis and review of the issues which are being dealt with in objection cases. We expect this work will be completed by March 2012.<sup>45</sup>

3.19 Relevantly, the SME Executive supported four aspirational measures on 30 April 2010. Among these measures, one aspiration is for objections to be legitimately upheld in taxpayer's favour in 20 per cent of cases. On 17 May 2011, the SME business line's Active Compliance Business Management Committee (AC BMC) met to discuss how to improve progress towards this aspiration. Among the relevant factors discussed at that meeting, was a need to improve the evidence to support technical positions and improve the relationship between the AC and IA areas.

3.20 The IGT believes that a level of caution is required in setting aspirations to have taxpayers' views upheld on objections in only 20 per cent of cases. Setting aspirational measures of this nature can sometimes drive behaviours that cause

---

<sup>44</sup> 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, p. 23.

<sup>45</sup> Australian Taxation Office, written communication to the IGT, 23 September 2011.

problems in other areas or merely shift the problem to another part of the process — see for example, the IGT's discussion of the two-year timeframe for large business audits in the IGT's Large Business Audit and Risk Review report. In the IGT's view, the aspiration should be recast to focus ATO officers on ensuring that initial compliance decisions are sustainable on external review — that is, that they are upheld when reviewed by the Administrative Appeals Tribunal and the courts.

3.21 The level of disputation with SME compliance decisions is too high. Improving the engagement between the SME business line's AC and IA areas would improve AC's awareness of common issues that give rise to increased disputation, afford AC an opportunity to make changes to avoid that disputation and minimise the imposition of unnecessary compliance costs on taxpayers.

3.22 In terms of early and alternative mechanisms to resolve disputes, such mechanisms should also be considered. The IGT will examine the use of such mechanisms in his review into the ATO's use of Early and Alternative Dispute Resolution (commenced in July 2011).

## **HWI OBJECTION WORK**

3.23 Objection work in the SME business line is done by IA officers. As at 30 June 2011, current staffing in the IA area is approximately 111 FTE staff, including administrative staff and management.

3.24 The work flows of objection work over the 2009–10 year are set out in appendix 2.

### **Quality of objections**

3.25 A recently commissioned ATO internal report observed that while SME was meeting its expected service standards on a quantitative basis, there were concerns when quality was considered:

[After recounting certain internal SME management reports] It is unnecessary to restate the results in these reports but it is useful to elaborate on some of the key issues identified in them. For example, it was immediately apparent that S&ME is meeting or exceeding most service standards, and workloads are being adequately managed. However, equally, there were many unanswered questions associated with the data when consideration was given to the qualitative assessment of the work as apposed to the quantitative measures.

The following summarises the key qualitative observations that can be gleaned from the metrics provided as part of this review:

- The stock on hand of IA and objection work is increasing. Interestingly, the increase in objection stock is not explained simply due to an increase in the number of objections received, but also due to a reduction in the rate of completions.

□ A significant number of objections are adjusted on objection (approaching 50 per cent). Although this figure may be alarming on face value because it suggests that audit cases are not being upheld during Objection – consideration needs to be given to the nature of the objection (for example, whether it relates to only part of the audit or only to penalties).

□ Aspiration targets are not being met – aspiration of 6 cases per FTE is currently at 5.18 per FTE. Aspiration of 20 per cent of objection adjustments is a challenge considering the results shown above.

□ The percentage of HWI objections to HWI audits has increased exponentially from July 2008 to March 2011 [In 2008–09, less than 5 per cent of HWI audits were objected to, however, in 2010–11, more than 20 per cent of audits were objected to].

□ Statistics suggest that IA HWI objections are being handled efficiently, with relatively low cost per unit in processing these objections when compared to objections still in HWI area, (however, there is no way to distinguish cases based on the complexity of the work).

Overall, the data analysis was useful and the inferences gleaned (above) from this data were consistent with the issues being raised by staff and the S&ME Executive.

The data is showing an increase in cycle times of objections and an increase in the number of objections being allowed (whether in part or full). The obvious concern is whether objection officers are unnecessarily ‘re-auditing’ the issues or indeed are not making best use of available resources (such as the STL and case leaders) to progress the objections.

In examining the concerns relating to cycle times and unfavourable objection rates, it becomes apparent that the reasons for delays in objections are related to many of the issues identified throughout this paper and addressed elsewhere – so it is unnecessary to repeat it here.

However, for the purposes of this section it is important to acknowledge that it is very difficult to make sense of the raw data to explain why these cases are not being managed effectively.

... Short of conducting a manual review of objections, it is difficult properly assess the reasons for this pattern of finalised objections. However, it is useful to outline some of the observations of possible contributing factors to the delays and unfavourable results of objections:

□ Quality of audits – there is anecdotal evidence to suggest that a number of audits leading to objection have poorly set out statement of facts, poor document management and a lack of a properly considered position ATO Position (sometimes due to protective assessments due to time constraints or assessment issued while audit still underway).

□ Issuing assessment while audit is still in progress – creates greater demand on objections officers.



□ STL officers not being used strategically — STL officers are engaged at the request of staff (by escalation) but there may be cases where leadership should appoint STL or STL proactively search for higher risk objection cases

□ Profiling capability levels of teams and allocating work appropriately — it is important that the capability and experience of IA and Objection teams are properly assessed and that this information is used to manage workflow.

There was no opportunity to collect evidence to test these assertions — however, staff were clearly concerned that these factors did contribute to the pattern of completed objections. The fact that these matters were raised in the course of the review would suggest that future case callovers attempt to focus on these matters.<sup>46</sup>

3.26 In the IGT's view, with respect to HWI compliance activities, the level of disputation, weight of objections upheld and the proportion of liability reversed on review indicate a high incidence of unsustainable initial ATO compliance positions. In a number of situations this is imposing very significant compliance costs on taxpayers for tax positions that on a more considered view should not have been raised. More work could be done to identify the reasons for initial compliance decisions not being upheld on review. Appropriate action needs to be taken to address those reasons.

## RECOMMENDATION 3.2

*The ATO should:*

- a. improve its initial compliance decision making capability to ensure sustainable decisions are made in the first instance; and*
- b. identify the reasons for initial compliance decisions not being upheld on review and take action to address those reasons.*

ATO response: Agree

Improving technical decision making remains a key priority for S&ME.

System based reporting to monitor and report on the outcomes of all objection cases has now been implemented. This reporting will be used to feedback into the audit process to ensure that our audit decision making is constantly improving.

## CONSIDERATION OF PART IVA ISSUES

3.27 The Case Leadership's call over report for the period March to May 2010, identified a trend of SME compliance officers regularly using Part IVA in cases and

---

<sup>46</sup> 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, pp. 15-19.

questioned whether alternatives had been properly considered. Case Leadership questioned whether:

- all other legislative avenues being properly considered by the case team before resorting to the Part IVA provisions?;
- some legislative provisions or ATO rulings so unworkable that the case team is only left with the option of pursuing Part IVA? (for example, issues with the application of IT 2450 in the Property, Building and Construction sector);
- the case teams have enough capability, or access to adequate support, to build a strong counterfactual? (Case Leadership made a conscious effort to ensure teams in the process of building counterfactuals were made aware of relevant avenues for assistance, including but not limited to, other case teams who have recently undertaken the process); and
- do TCN have an adequate level of resources to deal with so many Part IVA issues?<sup>47</sup>

3.28 In the IGT's view, there appears to be a number of general anti-avoidance rule (GAAR) matters considered by the ATO and the courts that raise a number of issues for the administration of the tax system. These issues are beyond the scope of this review, but the IGT may consider them in relation to his future work program.

## **EVASION**

3.29 Some private sector submissions to the IGT review claim that allegations of evasion are suggested by SME officers for several reasons, including as leverage to extend the periods for review. In an extreme example, one tax adviser claimed that SME officers asked for information outside the periods for review because of suspected evasion. In this case the taxpayer's Senior Counsel opinion supported the position adopted by the taxpayer, there was no penalty imposed by the ATO on the taxpayer and the ATO had earlier acknowledged that this was a case where two reasonable people could come to different conclusions.

3.30 The SME business line has a procedure of internally reviewing any conclusion of evasion before applying it in a taxpayer's case. Also, there are internal measures that require SME officers to refer any suspected fraud to the ATOs' Serious Non-Compliance (SNC) area. Also any cases that involve 75 per cent penalties are required to be considered for fraud referral.

3.31 The IGT notes that although conclusions of evasion are internally reviewed, suggestions of evasion are not. Some submissions commented that the suggestions appeared to be offered as a 'magic bullet' in lieu of other legal reasons. They also commented that SME officers making such suggestions did not appear to understand the evidence that was required to establish a finding of evasion.

---

<sup>47</sup> 'Summary note on S&ME Case Leadership Case Callovers', document attached to the agenda for the 30 June 2010 SME Executive meeting.

3.32 In the IGT's view, there is room to improve internal processes so that any suggestions of evasion are internally reviewed by senior officers before they are used as a reason — for example, to investigate matters occurring outside of the periods for review. Where evasion is suggested, a base level of documentation and evidentiary basis needs to be provided to the taxpayer. While the taxpayer may disagree with those allegations, at the very least, the taxpayer will understand the reasoning raised. If evasion is genuinely considered a risk by ATO senior management, the case should be referred to the SME technical panel for further action and the taxpayer notified of this action.

### **RECOMMENDATION 3.3**

*To improve internal processes dealing with suspicions of evasion, the ATO should:*

- a. ensure that any suggestions of evasion are internally reviewed by senior officers before they are communicated to taxpayers and/or used as a reason to investigate matters; and*
- b. in the event evasion is considered a risk by those senior officers, the case should be referred to the SME technical panel for further action and the taxpayer be notified of this action.*

ATO response: Agree

This is our current business process and we will ensure that all staff are aware of this and apply this process to their case work.

### **IMPROVING OFFICERS' TECHNICAL DISCIPLINE — USE OF THE FACTS AND EVIDENCE WORKSHEET**

3.33 Confidence in ATO technical decision making depends upon the ATO demonstrating it has based its decisions on cogent reasoning and relevant evidence.

3.34 The Facts and Evidence Worksheet provides a means to better focus compliance officers' attention on technical decision making including the legislative requirements, ATO administrative requirements, facts and relevance or application of evidence obtained. It provides a framework for officers to quickly narrow investigations to the evidence needed to robustly support technical decisions.

3.35 In February 2009, the SME Executive endorsed the rollout of the Facts and Evidence Worksheet for use in the following audit cases:

- cases likely to go to litigation;
- HWI cases;
- S4 cases; and
- more contentious cases.

3.36 There is no SME business line requirement for its officers to use the worksheet to formulate a position. The only requirement is that the worksheet be used to ultimately document the decision. This approach presents a level of duplication with other systems, such as Siebel, where facts and evidence is merely recorded. The SME Executive has asked that the integration of the worksheet with Siebel be further explored.

3.37 In late 2009, and following the IGT's settlement report,<sup>48</sup> the SME Compliance Leadership decided to make the Facts and Evidence Worksheet compulsory in all SME audit cases. The SME business line's Technical Excellence Practice (now subsumed into the STL area) reviewed SME officers' use of the Facts and Evidence Worksheet from November 2009.

3.38 In April 2010, the SME Executive were made aware of the findings of that review:

1.4 It is early days in the use of the worksheet but a number of general compliance case officers commented that they only use the worksheet because it is mandatory and do not see it as useful.

1.5 Most of the worksheets reviewed were incomplete and many were in the very early stages.

1.6 There are mixed views at this stage about whether the worksheet has improved the quality of fact and evidence collection and documentation.

1.7 According to most case officers, completing the worksheet is extending the cycle time for cases.

1.8 Better guidelines and training (using case studies and examples) on the use of the worksheet are required.

1.9 The format and headings in the worksheet could be improved to guide case officers and to provide a more useful and logical tool.

1.10 There appears to be a poor understanding of how to break down the elements of a legislative provision as well as what constitutes facts and evidence.

1.11 The worksheet at this stage does not appear to be used as anticipated except in a small number of cases that were completed very well.<sup>49</sup>

3.39 That review made a number of recommendations, including the following:

7.1 Worksheet training and guidelines

---

<sup>48</sup> Review into Aspects of the Tax Office's Settlement of Active Compliance Activities, October 2009, Sydney, available at [www.igt.gov.au](http://www.igt.gov.au).

<sup>49</sup> 'S&ME Facts & Evidence – S&ME Review of the use of the Facts and Evidence Worksheet in Audit Cases February 2010', p. 4, a document attached to the agenda for the 15 April 2010 SME Executive meeting.

- Develop and provide revised training and guidelines around use of the Facts and Evidence worksheet based on workshops and practical examples. Information and training is required on how to break down the elements of a legislative provision, what constitutes facts and evidence and how to document and reference that evidence.
- Follow up workshop based training for current case officers using case studies and examples.
- Build explanations of terms (for example, Facts) and provide simple examples into the worksheet itself. This could be done in the Heading fields.

7.2 Collect and provide good examples of completed and sanitised worksheets, for training purposes, and to provide feedback to case officers of the value of the worksheet.

7.3 Worksheet format and headings

- Review and improve format of worksheet so that fields align (for example, facts align with relevant evidence which then aligns with the relevant conclusions), columns automatically adjust for large sections of text This would improve the usefulness of the worksheet for quality review, decision making and transfer of information to position papers and Siebel.

7.4 Regular review of worksheets in progress by TEP members and team leaders. Worksheets to be reviewed at regular periods throughout their completion to provide feedback, assistance and timely rectification of gaps and issues.

7.5 Include review of the worksheet as an IQF [Integrated Quality Framework] requirement.

7.6 Develop a flexible approach to when and how the worksheet should be completed so that it is only being completed for the most important issues of the audit case.

The Facts and Evidence Worksheet has the greatest benefit if it is commenced at the stage when the case officer has a well developed risk hypothesis and when it is applied in a targeted fashion. That is, the case officer should focus the worksheet towards satisfying the most critical elements needed to prove their case. The other relevant undisputed elements only require a summary to show that they have been taken into consideration.

7.7 Conduct a second review of the use of the facts and evidence worksheet in 6-12 months.

... 7.9 The S&ME Executive to champion the benefits and value of the Worksheet to S&ME Audit staff.<sup>50</sup>

3.40 At the 15 April 2010 SME Executive meeting it was observed that the worksheet 'was very helpful when dealing with objections and has the ability to

---

<sup>50</sup> Ibid, pp. 13-14.

improve our dispute resolution, if done properly' especially when 'a lot more HWI taxpayers appear to be challenging amendments'.<sup>51</sup>

3.41 Additionally, some private sector submissions set out a number of examples in which it is claimed that SME officers demonstrated a lack of appropriate consideration of issues and/or legislation. Among other things, they claim that an overly onerous evidentiary burden was placed on taxpayers in some areas.

3.42 In the IGT's view, improving discipline in dealing with the evidentiary basis for active compliance decisions (including primary tax and penalty decisions) would improve the sustainability of SME compliance decisions. Using the Facts and Evidence Worksheet as a means to formulate views would likely improve the overall level of technical decision making, generally narrow the scope of information requests, facilitate a focused and evidence-based discussion with taxpayers on the issues with a view to establishing a shared understanding of the strengths and weaknesses of each parties' case, improve overall dispute management and reduce the number of objections.

#### **RECOMMENDATION 3.4**

*To improve the evidentiary basis for compliance decisions, the ATO should require SME officers to use the Facts and Evidence Worksheet to:*

- a. guide their inquiries and formulate views from the point at which a risk hypothesis has been developed through to the finalisation of position papers;*
- b. improve SME officers' (including those who sign off on compliance officers' work):*
  - i. ability to break down the elements of a legislative provision;*
  - ii. to determine what constitutes facts and evidence;*
  - iii. how to address conflicting pieces of evidence*
  - iv. that affidavits are a form of evidence; and*
  - v. what level of evidentiary burden is appropriate; and*
- c. update worksheets as new information comes to light.*

**ATO response: Agree**

---

<sup>51</sup> Minutes to the 15 April 2010 SME Executive meeting, p. 2.

## INTEGRATED QUALITY FRAMEWORK'S (IQF) ASSURANCE OF WORK QUALITY

3.43 The ATO's IQF comprises six interrelated processes aimed at improving and assuring quality, including the quality assessment of compliance decisions.

3.44 IQF case assessors review all finalised penalty decisions and a sample of SME compliance cases, both finalised and in progress. There are local case assessors on site. The IQF team is aiming to develop dedicated HWI case assessors.

3.45 In relation to finalised or 'closed' cases, the IQF process involves randomly selecting a number of audits and reviews (in accordance with Australian Bureau of Statistics advice). They are not stratified according to taxpayer type or turnover. With HWI cases, the case assessor must physically sit with the case officer linked to the particular case because of systems access restrictions. This means that the IQF team relies on HWI officers to do the case assessment of their colleagues.

3.46 In relation to cases in progress or 'open' cases, case assessors aim to identify opportunities for improvement before final sign-off. Cases are selected from a cross section of risk projects and geographical spread. The assessment is done by the team leader and therefore will not identify any gaps in the team leader's knowledge.

3.47 The IQF team checks the case assessor's work by checking whether the rating matches the comments in the case report. They do not check whether there is evidence for the case assessor's comments.

3.48 In the IGT's view there is room to improve IQF reviews of SME officer's work, including in the following areas:

- ensuring IQF review of S4 and HWI cases is done by experienced senior technical officers with expertise in S4 and HWI work;
- stratifying IQF reviews according to the different population segments of the SME market;
- improving case assessors' access to HWI cases for independent review; and
- involving senior officers in open case reviews.

### RECOMMENDATION 3.5

*The ATO should improve IQF reviews of SME work, including:*

- a. ensuring IQF review of S4 and HWI cases is done by experienced senior technical officers with expertise in S4 and HWI work (such as Case Leadership);*



### **RECOMMENDATION 3.5 (CONTINUED)**

- b. stratifying IQF reviews according to the different population segments of the SME market;*
- c. improving case assessors' access to HWI cases for independent review; and*
- d. involving senior officers in open case reviews.*

**ATO response: Agree**

**Our IQF processes now include these items.**



## CHAPTER 4 — PROJECT MANAGEMENT

4.1 The SME business line has as a substantial number of processes and mechanisms to assist with project management of active compliance activities and related programs (such as objection and litigation arising from those activities).

4.2 Submissions to the review expressed dissatisfaction with the project management of many compliance activities. Areas of concern related to the timeliness of compliance actions and degree of communication with SME compliance officers and supporting technical staff to ensure that expectations were shared.

4.3 Notwithstanding the ATO's processes and mechanisms, the review identified further room to improve project management in relation to resourcing, end-to-end case reporting, cycle time flexibility, effectiveness of upstream risk identification processes, automated linking systems, proactive case management and staff understanding of processes and structural changes. These areas are discussed in more detail below.

### GOVERNMENT FUNDING AND ATO ALLOCATIONS

4.4 Submissions raised a number of concerns with the ATO's project management, including concerns that the level of ATO internal funding allocated to its SME activities may not be adequate to properly resource its intended activities. These submissions raised concerns that the ATO's allocation may affect the quality of interaction between SME officers and taxpayers and their advisers.

#### SME business line concerns

4.5 Although the SME business line has been allocated funding to conduct the HWI expansion, S4 risk review and WA initiatives, it has expressed concerns in its 2010 Health of the System Assessment (HOTSA) in delivering commitments over the medium and longer term:

Are the right resources in the right places to achieve our present and future outcomes?

□ In 2010-11, we allocated resources to meet our compliance commitments and revenue targets. We have concerns about our ability to deliver future outcomes associated with the Income Tax Investment and HWI programs in the medium to longer term. This concern is compounded by commitments outlined in the 2009 Federal budget around the 'Wealthy Australians' project.

□ The 'Wealthy Australians' project is a cross-business line initiative employing both S&ME and ME&I staff. A continuing large capability build is necessary to equip staff with an understanding of our 'private group' approach. HWI and General Compliance staff have joined these teams to mentor new staff and support structured learning using our Integrated Capability Development System and learning pathways to fast-track capability gains.

□ HWI and General Compliance staff have represented logical recruiting pools as the 'Wealthy Australians' project has expanded. This may create consequential capability issues in light of escalating HWI and Income Tax Investment targets. This is particularly relevant for HWI which also needs to cope with a significantly larger HWI population.<sup>52</sup>

## Governance at the macro level and the ANAO review

4.6 Overseeing the governance development and management of the SME business line's program of work is a business management structure, comprising seven strategic and ten operational committees (not including regional leadership groups) with different foci, and related reporting.

4.7 The Australian National Audit Office conducted a review of the ATO's management of compliance in the SME market, including an examination of case management which focuses heavily on governance at the macro level. Therefore, the IGT has not sought to examine this aspect of the SME business line's operations.

## INCREASED TECHNICAL RESOURCES

4.8 The increased compliance activity carried out by the SME business line will place further demand on the SME business line's technical resources, as well as the COEs and the TCN.

4.9 Within the SME business line, technical support resources have been increased from 30.49 FTE staff in 2006-07 to 47.24 FTE staff in 2009-10. The SME business line's Case Leadership area has been increased from 4.58 FTE staff in 2006-07 to 9.04 FTE staff in 2009-10. The Case Leadership area is fully funded from HWI new policy funding.

4.10 The COEs and TCN were collectively allocated \$4.89 million of the HWI funding (from 2006-07 to 2009-10), and \$11.3 million from the Income Tax Investment (ITI) and Strategic Compliance Initiative funding. However, this funding to the COEs and TCN is not directly linked to any SME business line activities and is expected to fund increases in other business lines' workloads as well, such as the LBI business line.

4.11 In the IGT's view, it would be helpful to demonstrate how much of the HWI, ITI and Strategic Compliance Initiative funding allocated to the COEs and TCN has resulted in tangible benefits to the SME business line.

### RECOMMENDATION 4.1

*The ATO should develop indicators to measure how funding allocated directly to the COEs and TCN results in benefits to the SME business line.*

---

52 'S&ME Income Tax HOTSA 2010 — Compliance Sub-plan Health of the System Assessment (HOTSA)', p. 28, document attached to the minutes of the 16 September 2010 Risk Management Committee meeting.

ATO response: Agree

As part of the TTDM project a full review of the usage and effectiveness of CoE and TCN resources will occur in order to determine the level of any shift of resources or priorities.

## ACTIVE COMPLIANCE CASE END-TO-END REPORTING

4.12 The ATO has systems that provide snapshots of aggregated cases at certain points in time. Any work to examine the downstream or upstream action (for example, active compliance, objections, litigation) on cases must be done manually. The ATO does not have an automated system which provides end-to-end reporting on individual case workflows.

4.13 However, the SME business line does examine the results of flows of cases within the suite of differing active compliance products, namely 'case sequencing charts'. These case sequencing charts show the output of completed active compliance cases and set out how cases progressed through different active compliance activities. These charts, however, do not link to or examine any downstream activities, such as any objections or appeals, or reconcile liabilities raised with that reversed later.

4.14 The IGT considers that much could be gained from extending the case sequencing charts to include downstream dispute resolution steps and obtain an end-to-end picture of cases. Much could also be gained from capturing downstream ATO costs (such as objection and litigation work) as well as estimated taxpayer costs in conducting the activities to obtain an understanding of the broader economic impacts of SME compliance activities.

### RECOMMENDATION 4.2

*For the purpose of obtaining end-to-end analyses of completed compliance cases, the ATO should extend the use of its 'case sequencing charts' to capture:*

- a. the reversal of liabilities in the cases' downstream dispute resolution steps;*
- b. the ATO's costs in the cases' downstream dispute resolution steps; and*
- c. estimated taxpayer costs for the total activities in cases (that is, cases' active compliance and downstream dispute resolution steps).*

ATO response: Partially agree

We will implement the development work currently underway to provide full Siebel based reporting on compliance case outcomes where disputes are lodged. Reporting for cost of the ATO's downstream activity is already available using ATO Unit Cost Analysis data. This data is currently used by the interpretative assistance area to measure the cost of its range of products.

Whilst we are always mindful of the cost of compliance for taxpayers we do not intend to develop a process to estimate taxpayer costs in relation to S&ME compliance activities. It would be extremely difficult and potentially misleading to make valid estimates as all taxpayers would have different cost profiles dependent on their specific circumstances, the complexity of the matters being reviewed or audited and the cost of seeking advice and representation from advisers.

## **CYCLE TIMES FOR ATO ACTIVITIES**

4.15 The ATO's expected timeframes for completing active compliance activities (cycle times) depend upon the type of activity (or 'product') undertaken.

4.16 Many submissions perceived that ATO internal deadlines appeared to influence some SME officers' behaviours – for example, one submission commented that when no deadline was looming an auditor may 'drag their feet', however, when there was a deadline looming an auditor may impose unrealistic timeframes for the taxpayer's response.

4.17 Submissions received from certain ATO staff observed that cycle times in S4 risk reviews were too short to properly assess the risks within the timeframes expected, leading some to 'cut corners' to meet their targets. In any event, these cycle times in S4 cases may have been too short for less experienced officers to properly consider the potential risks.

4.18 The SME business line has since reviewed its cycle time for audit and review products. On 25 August 2010, the SME Executive agreed to that review's recommendations to change cycle times and products. In considering the cycle times the review recommended:

1 Maintain IT [Income Tax] SME Comprehensive Audit and IT HWI Comprehensive Audit

... maintain two Audit Field case products; 730 and 540 day cycle times

... The need to retain an audit product with a 730 day cycle time reflects the long delays experienced for the more complex cases, particularly in regard to cases involving international issues where information requests are made from overseas entities and when dealing with very complex technical issues which often involve delays in obtaining legal advice for ourselves and the taxpayer

... 2 Maintain IT SME PRR [Preliminary Risk Review]

☐ It is recommended to maintain the IT SME PRR to fulfil the S4 project commitments, as well as now being used as BAU [Business As Usual] across the line

☐ It is recommended that this case product be reviewed in view of decreasing the cycle time once efficiencies can be identified as a result of the Front End Operations initiative

... 8 Park IT SME Comprehensive Risk Review [CRR]

- This case product meets the 120 day cycle time only 52 per cent of the time
- The Private Wealth Approach will increase the number of entities in the Group under review and it is therefore expected to take longer to complete
- Staff have consistently told us that 120 days is too short, taking into consideration waiting times for responses from taxpayers, particularly when extensions are granted (which is very often), issues around time delays resulting from taxpayers wishing to make Voluntary Disclosures etc.
- It is recommended to create a new case product that combines this case product and the HWI CRR with a proposed cycle time of 180 days

#### ... 9 Park IT HWI Comprehensive Risk Review

- It is evident that HWI can make improvements in case management practices
- When combined with the Preliminary Risk Review product the total amount of time allowed for the identification of risks is 300 days, which is considered to be too long
- 240 days in total is considered to be adequate for the identification of risks; hence a 180 day cycle time for Comprehensive Risk Reviews
- It is recommended to create a new case product that combines this case product and the GC CRR with a proposed cycle time of 180 days.<sup>53</sup>

4.19 The following table sets out the current times for completing the relevant SME active compliance activities. 'Direct time' means the time the staff member spends on the case. 'Cycle time' means elapsed time to complete the activity.

---

<sup>53</sup> 'S&ME Case Product Reduction and Cycle Time Recommendations, pp. 2-5, document attached to Minutes of the 25 August 2010 SME Executive meeting.



**Table 2: SME products by direct and cycle times**

<b>S&amp;ME Siebel Products as at 18 April 2011</b>			
<b>Current Siebel Product Names</b>	<b>Comment</b>	<b>Direct Time</b>	<b>Cycle Time</b>
<b>Internal Reviews</b>			
IT SME Internal Review		12 hours	40 days
<b>Specific Reviews</b>			
IT SME PRR		8 hours	60 days
IT APA ACR HV	Only for International cases		60 days
IT SME SR Corr HV		8 hours	60 days
IT SME SR Corr		8 hours	60 days
IT Voluntary Disclosure		2 hours	40 days
IT Ind tax haven review HV	Only for International cases	9 hours	90 days
<b>Comprehensive Reviews</b>			
IT SME Comprehensive Risk Review		15 days	180 days
<b>Specific Audits</b>			
IT SME Office Specific Audit		41 hours	180 days
IT SME Spec Audit Corr HV			60 days
<b>Comprehensive Audits</b>			
IT HWI comprehensive audit	Only for Wealthy Australian & HWI	300 hours	730 days
IT SME Comprehensive Audit		62 days	540 days
<b>Agreements</b>			
IT complex APA	Only for International cases		730 days
IT simplified APA	Only for International cases		270 days
IT standard bilateral APA	Only for International cases		730 days
IT standard unilateral APA	Only for International cases		360 days

Source: Australian Taxation Office

4.20 For objections, the ATO states that it expects to finalise 70 per cent of objections within 56 days of receiving all information requested, or in complex cases within the due date negotiated with the taxpayer.

4.21 The SME business line monitors on a monthly basis the percentage of SME cases that are completed within the relevant cycle times. As at 25 March 2011:

- the GC area has been tracking at 76.9 per cent cases being finalised within the expected cycle times, with 74.3 per cent of cases on hand still within cycle times;
- the HWI area has been tracking at 67.3 per cent cases being finalised within the expected cycle times, with 69.6 percent of cases on hand within cycle times; and
- the WA area has been tracking at 81.1 per cent cases being finalised within the expected cycle times, with 62.2 per cent of cases on hand still within cycle times.

4.22 In the IGT's view, care must be taken in setting cycle times for compliance staff. As the IGT has observed in the large business audits review,<sup>54</sup> cycle times for completion may drive behaviours that cause other problems that are difficult to resolve. The SME business line should enable SME officers to extend the cycle times in appropriate circumstances, without adverse impact on management's view of the SME officer and whilst minimising the adverse impacts on the taxpayer. Where these time

<sup>54</sup> Inspector-General of Taxation, Report into the Australian Taxation Office's large business risk review and audit policies, procedures and practices, Sydney, May 2011, available at [www.igt.gov.au](http://www.igt.gov.au).

frames are extended, ATO staff should (as is recommended in Chapter 5) communicate these changes to the taxpayers.

4.23 The IGT is strongly of the view, that the ATO risk review and audit approaches should be designed to minimise unnecessary compliance burdens on taxpayers. It is also important to ensure the likely taxpayer compliance burden is proportionate to the revenue risks involved. The SME business line's extension of cycle times for S4 risk review products by another 60 days may help to reduce some of the behaviours that caused taxpayers and their advisers concern. However, any extension in cycle times should be balanced against the adverse impacts on taxpayers. The ATO should continue to monitor the effectiveness of these cycle times over the range of its products and, in doing so, inform itself of the views of taxpayers and advisers who were involved in the compliance cases.

### **RECOMMENDATION 4.3**

*In order to appropriately minimise unnecessary compliance burdens on taxpayers and their advisers, the SME business line should:*

- a. continue to monitor the effectiveness of cycle times over the range of its compliance products and, in doing so, inform itself of the views of taxpayers and advisers who were involved in the compliance cases; and*
- b. enable SME officers to extend the cycle times in appropriate circumstances, without adverse impact on the taxpayer.*

#### **ATO response: Agree**

We review product cycle times annually and adjust as necessary.

We will use feedback from our S&ME ATO Tax Practitioner Forum in this process.

We will reinforce the current policy where case officers, in discussions with their team leaders, can extend the cycle time of a case where appropriate and, where it is ATO initiated, ensure that the taxpayer understands the reasons and is not adversely impacted.

### **HWI TASKFORCE WORKFLOWS**

4.24 The SME business line advised the IGT that for the purpose of resource allocation it estimates 50 per cent of PRRs become CRRs and 30 per cent of CRRs escalate to audit. In the 2009-10 year, the case sequencing charts disclose that the percentage was closer to 40 per cent (203 out of 342 PRRs were not escalated for further compliance action).

4.25 For the 2009-10 year, the HWI taskforce area completed 514 cases. On the basis of the case sequencing charts for that year, there have been a number of unproductive active compliance products in terms of protecting revenue and

minimising compliance costs. On the basis of the figures in these charts, initial PRRs provide wider coverage at a lower cost to the ATO. As cases escalate to CRRs and audits, the costs increase and so do the strike rates and liabilities raised. The following table summarises those charts.

**Table 3: Summary of HWI case sequencing charts for the 2009–10 year**

Initial type of case (first in sequence)	Number of completed cases	Cases with compliance result	Liabilities raised in \$m	Notional tax reversed in \$m	Cost to ATO in \$m	Strike rate	\$ return per \$1 of ATO cost
Field audit	6	6	136.1	0	0.468	100.00%	290.81
PRR	343	37	31.264	86.6	4.619	10.79%	25.52
CRR	65	21	17.8	9.4	2.92	32.31%	9.32
Internal Review	89	4	22.03	0	1.812	4.49%	12.16
Specific Inquiry	21	2	0.06	0	0.574	9.52%	0.10
Other	13	1	0.03	0	0.178	7.69%	0.17
Voluntary Disclosure	5	5	2.5	0	0.017	100.00%	147.06
Total	542	76	209.784	96	10.588	14.02%	28.88

4.26 The HWI case sequencing data indicates that only certain types of sequences lead to amended assessments, or a direct compliance result. In the IGT's view, this implies that other non-productive activities are imposing a disproportionate compliance burden on compliant HWI taxpayers. This indicates a need for further SME business line work to assess the effectiveness of its upstream risk identification processes in targeting likely non-compliance and reducing compliance costs on compliant taxpayers.

#### **RECOMMENDATION 4.4**

*The SME business line should assess the effectiveness of its upstream risk identification processes in targeting likely non-compliance and reducing compliance costs on compliant taxpayers. In conducting this assessment, the SME business line should inform itself from the analysis of the case sequencing charts and analysis of objections cases.*

ATO response: Agree

We are implementing a risk differentiation framework (RDF) which will apply across all populations within the S&ME and private wealth markets. This process will support a differentiated compliance approach dependent on our assessment of the risk for each taxpayer.

We will use Siebel case data to determine NFA and early exit rates and feed that data back into the RDF and case selection processes to improve these processes and assist to minimise unnecessary case work.

## INCOME TAX INVESTMENT (ITI) — S4 MARKET SEGMENT WORKFLOWS

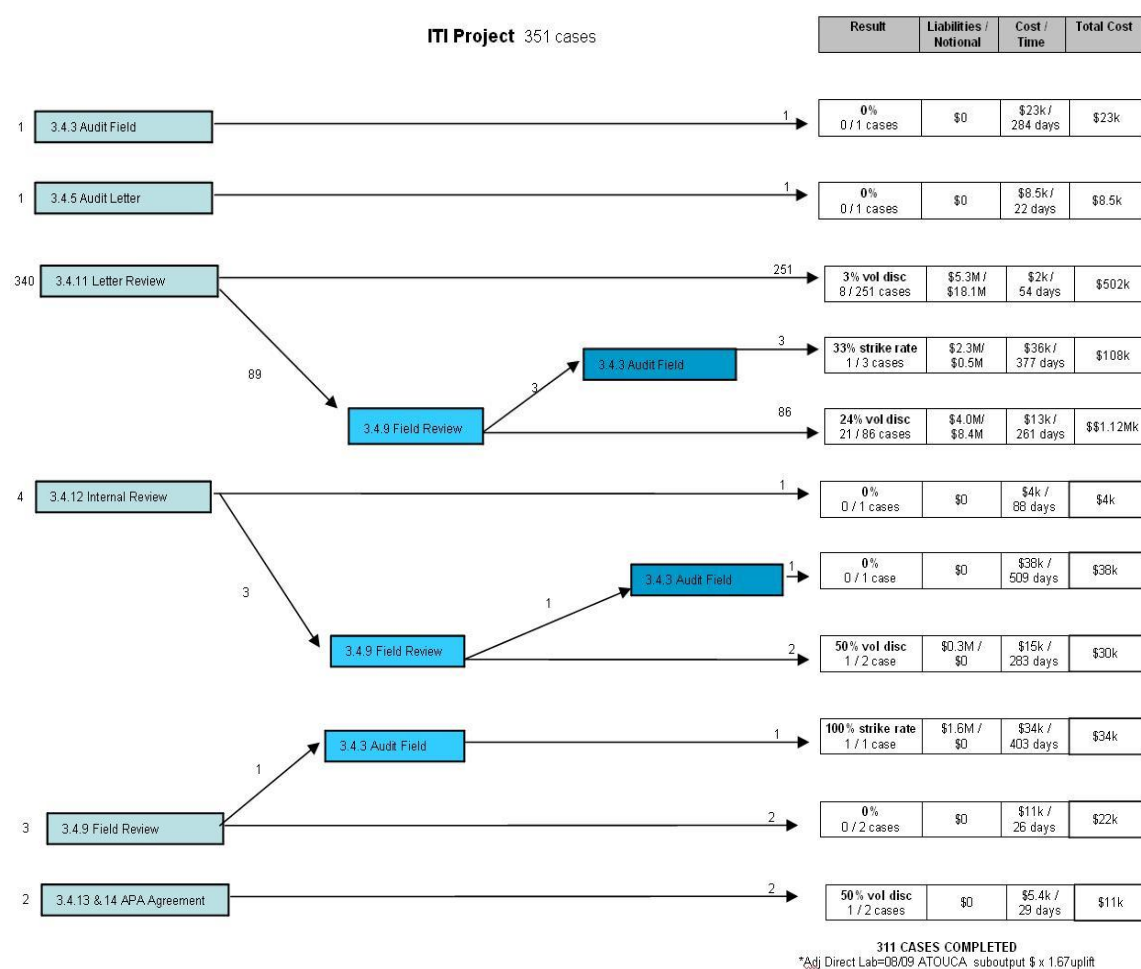
4.27 As stated in chapter one, the SME business line's contribution to the ITI is, over four years, to risk review all S4 taxpayers, raising \$350 million in direct revenue and \$630 million in indirect revenue. It started on 1 July 2008.

4.28 The SME business line has based delivery of its contribution to the ITI on the following workflow estimates: a total of 1400 cases, 60 per cent will not progress further than the PRR stage and 60 per cent of cases at the CRR stage will not progress to audit.<sup>55</sup>

4.29 The following case sequencing charts show the SME business line's S4 cases for the 2009–10 year.

**Figure 1: S4 market segment case sequencing charts for the 2009–10 year**

S&ME GC ITI PROJECT CASE SEQUENCING FOR TOTALLY CLOSED CASES – 1/07/2009 to 30/06/2010



Source: Australian Taxation Office

4.30 The number of cases reviewed in the 2009–10 year represent approximately a quarter of the taxpayer population in the S4 market segment. In summary, the SME

55 Australian Taxation Office, presentation to IGT staff, May 2010.

business line raised \$12.2 million in direct liabilities and \$27 million in notional tax protected in 33 out of 351 cases for a total cost to the SME business line of just over \$1.9 million.

4.31 Just under three-quarters of the total number of cases received a lower level of scrutiny from the SME business line (letter review) at a lower cost to the SME business line (\$2000 per case), with just under one-quarter receiving an increased level of scrutiny (field review) at a mid-range cost to the SME business line (\$13,000 per case). Less than one per cent of cases resulted in field audit with the highest cost to the SME business line (approximately \$36,000 per case). Note that the cost to the SME business line only includes compliance staff, not technical officers, case leadership, objections staff or other ATO areas that may be involved in the case.

4.32 As at February 2011, a performance report to the SME Executive stated that for the year to date (as at 24 February 2011):

- General Compliance Income Tax Investment (S4) commitment comprising of \$120 million revenue \$70 million cash and indirect revenue of \$150 million. This commitment will be measured using a combination of the ITI project and the broader program including S4 market cases. A review of the audit case outcomes in the S4 (ITI) segment during February 2011 is indicating that liabilities are currently tracking below has been planned for 2010/11. While cases numbers are on track liability outcomes are not as strong as predicted for 2010/11 when they were put in place by the original ATO funding proposal for this body of work. We expect a shortfall in planned direct S4 liabilities in 2010/11 of around \$30-\$40 million based on \$120 million original planned outcome for this segment. In terms of indirect revenue planned for the S4 segment RAB [Revenue Analysis Branch of the ATO] has endorsed S&MEs methodology for measuring this outcome and have accepted that to date the program has delivered between \$200 million and \$300 million in indirect revenue as a result of our engagement and overall activity within this segment.

... We have invested significant senior resources in the risk assessment and review processes for the S4 work and we are confident that the best cases are progressing to audit and that our audit outcomes are sound.<sup>56</sup>

## **WEALTHY AUSTRALIANS (WA) PROJECT**

4.33 The ATO's WA project aims to raise, over a four-year period, \$285 million tax liabilities and collect \$170 million of these liabilities.

4.34 The SME business line has based delivery of its contribution to the WA project on the following workflow estimates: a total of 75,000 potential cases, 40 per cent will not progress further than the *Private group structure questionnaire* stage (these questionnaires are discussed further in chapter 6). The ATO has since reported that there are approximately 82,000 potential cases.

---

<sup>56</sup> 'S&ME Active Compliance — performance report: year to date 24 February 2011', pp. 5-6, prepared for the SME Executive.

4.35 This project is in the early stages of its roll out.

## PROJECT MANAGEMENT OF CASES

4.36 The ATO's 'IPEC' model (which stands for Initiate, Plan, Execute and Close) comprises a high level methodology to project manage case work.

4.37 An SME business line workshop with externals identified that 2 of 8 cases examined were not progressed because of the lack of proactive case management.<sup>57</sup> The external representative recommended that 'training be provided to ensure case officers understand the importance of continual monitoring and re-communicating with the taxpayers to ensure the cases are completed within a timely manner'.<sup>58</sup>

4.38 A later workshop<sup>59</sup> examined the deeper cause for case plans not being followed. It identified that a level of staff disengagement and knowledge impeded the escalation of errors and problems with procedures and their timely updating. Opportunities for improvement were identified. These were to develop escalation processes for staff, to provide a gateway for the maintenance of current and accurate procedures around case plans and to utilise internal communication networks to reinforce the requirement to complete case plans (while this is not a root cause of the issues around case plans, it has been identified as a solution to improve staff awareness for the procedures of case plans).

4.39 In the IGT's view, the SME business line could do more to ensure SME officers proactively manage cases, including the continual monitoring, re-communication with taxpayers and complying with the requirement to complete case plans before commencing activities.

### RECOMMENDATION 4.5

*The ATO should improve management oversight and assurance measures to ensure SME officers proactively manage cases, including continually monitoring cases, re-communicating with taxpayers and complying with the requirement to complete case plans before commencing compliance activities.*

#### ATO response: Agree

We will implement the Compliance Active Case Management project outcomes which are being rolled out across the compliance sub plan during 2011/12.

We will also reinforce the need for case officers to prepare a case plan and discuss this with the taxpayer at the outset of the case.

---

<sup>57</sup> The SME business line's Community Involvement Workshop, 27 August 2010.

<sup>58</sup> 'Small and Medium Enterprises (SME) Active Compliance (AC) Integrated Quality Framework (IQF) Community Involvement Workshop (CIW)', a document prepared by the community representative on the SME business line's Community Involvement Workshop, 27 August 2010.

<sup>59</sup> The SME Active Compliance Continuous Improvement Workshop, 17 September 2009.



We have implemented a 'checkpoint reporting' process to assist managers to monitor the progress of cases.

## SYSTEMS SUPPORT

4.40 Internal ATO research identified that an SME system, called 'BMT', was not linking related taxpayer entities together properly, thereby increasing SME officers' time taken in manually establishing links and increasing the risk of less experienced officers missing links with other entities.

4.41 The potential impact of this on taxpayers is the potential duplication of risk reviews for the same economic group, creating unnecessary increased taxpayer compliance costs.

4.42 The SME business line identified the ability to link entities as a key risk in its 2010 HOTSA:

What are the key risks to our internal capability?

...□ Data collection / systems – Within S&ME we are focusing on closely held private wealth groups that link entities to the economic group / controlling mind. This focus was derived from the systems and processes developed within the HWI taskforce. Increasingly for S&ME, we are developing new views on our information and data to support this changing approach. Through this work we have been experiencing issues with data warehouse speed and accessibility. We are working with [other areas of the ATO] to ensure performance and support for the business demands is maintained for our critical business needs.<sup>60</sup>

4.43 In the IGT's view, improving the identification of links between related entities within the same economic group will help to reduce compliance costs on taxpayers in responding to unnecessary information requests.

### RECOMMENDATION 4.6

*To reduce the risk of duplicating risk reviews for the same economic group, the ATO should improve its automated systems' ability to identify links between related entities within the same economic group.*

#### ATO response: Agree

We have been investing significant resources into our processes for collecting data and linking entities to economic groups and to individuals to assess their net wealth. This work continues to produce improved outcomes for linking entities.

---

<sup>60</sup> 'S&ME Income Tax HOTSA 2010 - Compliance Sub-plan Health of the System Assessment (HOTSA)', p. 30, document attached to the minutes of the 16 September 2010 Risk Management Committee meeting.



## **INTERPRETATIVE ASSISTANCE (IA) AREA'S RESOURCING**

4.44 In addition to concerns with the delivery of outcomes, specific concerns were raised in relation to the resourcing of the SME business line's IA function.

4.45 During the review, the ATO commissioned an internal review to examine what changes may be needed given the expected shift in compliance work type and workloads. Among other things, that report considered a specific area where resourcing was said to be insufficient:

There were claims made that IA was not sufficiently resourced to carry out its work, particularly in relation to HWI objection work. All sites indicated they were working at near full capacity and any sudden increase in work would be difficult to manage. ... clearly there are resource pressures in IA that need to be managed. It appears that S&ME management have long recognised the need to resource this area but for various reasons it has not been able to make it happen.

### **Recommendation 6**

Urgent action is taken to fill positions in IA to deal with increasing workloads.<sup>61</sup>

4.46 In examining the underlying reasons, the report considered the basis upon which workloads were calculated:

[The then Deputy Commissioner of the SME business line] mentioned at a Governance session that he would like to see IA officers moved towards completing six cases a month. This was calculated at 60 per cent of 20 working days a month (12 days per month), and estimating that case officers should be able to do one case every two days – for a total of six cases per month. There was an expectation that S&ME would increase productivity (that is, case holdings per officer) in order to achieve this aspiration.

However, since then the compliance program has significantly changed ... and the IA area is starting to face pressure in handling objections to more complex issues. Consideration needs to be given to whether case work needs to be categorised. The aspiration of 6 objections per FTE per month is probably achievable for routine cases but is clearly not feasible for complex objections.<sup>62</sup>

## **Restructuring of objections function**

4.47 In considering this issue it is also important to understand the background to the SME business line's IA function and the restructuring of its objections function.

4.48 In 2009, HWI objections were dealt with by different ATO teams to those that dealt with SME objections. At the 24 November 2009 SME Executive meeting, it was decided to centralise the HWI IA functions and transfer that function to the SME IA

---

61 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, p. 21.

62 Ibid, pp. 26–27.

area by 1 July 2010. At the time, HWI IA work was done by 9 FTE staff in the HWI AC teams and Technical Excellence Practice (now subsumed into the Senior Technical Leadership).

4.49 Based on a predicted increase in HWI audit activity it was estimated that approximately 26–35 FTE staff would be needed to manage expected HWI IA work. However, the SME Executive would consider their agreement to that expected FTE staff increase in May/June 2010 when it could be determined what resources would get freed up as a result of this integration and the outcome of other productivity initiatives. A staged approach to implementation of the restructuring was ultimately decided upon, with savings expected to arise from the integration. However, as later events show, the integration did not reduce the workloads for IA staff.

### **Staff concerns with resourcing and management's response**

4.50 By mid-2010, senior SME officers were made aware of more junior officers' concerns with the IA area's resourcing. In March/April 2010, the SME business line conducted feedback sessions with its officers with 85–90 per cent attendance. Amongst other comments that SME business line officers 'consistently raised across various sites and sessions', they commented that:

#### Technical area merger

- Comments centred around this move being beneficial, and in line with a private wealth approach. Most sites with an IA presence commented that they are pleased to see this, as they felt the current technical support in IA is not adequate.

#### ...Interpretative Assistance

- Some IA staff are feeling heavily criticised at the moment (for example, criticisms of their productivity and inaction on Siebel issues that cause them to fail cycle times)
- Technical support for IA was raised several times. The new technical area will assist in addressing some of this issue — but it is something we may need to consider moving forward.<sup>63</sup>

4.51 It also appears that there were significant work pressures in at least one IA site, requiring Human Resource practitioner involvement and active involvement of Assistant Commissioners.

4.52 The SME Executive had agreed to find 10 more FTE staff to transfer from the HWI area to the IA area as soon as possible. However, as at 1 June 2011, this action item was not complete. A recently completed ATO internal report also recommended urgent action be taken (see above).

---

<sup>63</sup> 'Feedback from SME Information Sessions March/April 2010', p. 2, document attached to the agenda for the 12 May 2010 SME Executive meeting.

## Gap in resources at main IA site

4.53 A recently completed ATO internal review of the IA area identified a gap in IA resources in one of the main sites:

... it is understood that the Box Hill site that is principally responsible for HWI objections, has had a number of staff relocate out of S&ME, and this has left a significant gap in resources within Box Hill IA. It would not be wise to simply replace these staff with new recruits and expect them to continue to carry out HWI objections. Indeed, the fact that this site is remotely managed by a director in Adelaide and the SES in Perth is further reason to consider the nature of the work this team should be doing. There should be no reason why HWI objections could not be handled in other sites within Melbourne. The work should go to more established teams (who have the capability and experience to handle the work) or alternatively Box Hill should be resourced by experienced staff (who understand the S&ME business and have the capability to handle complex work).

Consideration needs to be given to whether the Box Hill IA site needs to be relocated or whether its workload should be reassessed.

### Recommendation 5

Box Hill site needs to be resourced with experienced SME staff who can handle complex HWI work or, alternatively, consideration be given to the feasibility of keeping an IA/objection site in Box Hill where there is limited site leadership to handle these complex cases.<sup>64</sup>

## Sharing information to help predict the IA area's workloads

4.54 The ATO's internal report also observed that there may be information needed to predict downstream workloads (such as objections) which may not always be shared within the business line:

It is understood that IA areas have access to AC's [the Active Compliance area] data on 'work in progress' and 'expected completion' ... which assist in planning for projected workloads. Also, the IA area has recently completed work for an IGOT review on finalisation outcomes for audit objections. Reports such as these provide valuable information in relation to expected workloads, complexity of issues and capability of workforce – which is necessary for positioning and planning for IA functions.

In the course of meeting with various directors it became apparent that there are some reports prepared by AC that the IA area was not privy to. It is unclear what reports are routinely available to IA to assist them with the projections and planning for IA work.

---

<sup>64</sup> 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, pp. 18-19.

## Recommendation 7

AC management reports and IA management reports should be routinely shared with each other. Consideration should also be given to joint reports that are prepared for the purpose of BMC committees.<sup>65</sup>

4.55 Relevantly, the ATO advised the IGT during the review that:

We will design and build a 'complexity measure and indicator' into our case selection process to enable us to better understand the nature of case work we plan to undertake. The indicator will also provide us with a better basis for planning our resource needs and allocation of the correct resources to match the case work. We plan to have this in place for the 2012/13 year.<sup>66</sup>

4.56 In the IGT's view, the ATO's compliance focus on more sophisticated taxpayers is likely to lead to more complex cases being considered and increased potential for disputation. On this basis, the ATO should undertake to reassess, and carefully monitor, its resourcing allocation for the pipeline of compliance work (including dispute resolution functions, such as objections and litigation). The ATO should ensure that the SME business line's IA areas are sufficiently resourced to appropriately handle the number and complexity of objections being lodged. In line with recommendations 5–7 of its internal report, the ATO should act to fill gaps in resourcing (such as that identified above) as well as ensure that relevant information is shared within the business line. The IGT also considers that the SME business line should also more broadly carefully reconsider its current staffing, capabilities and management of its IA areas in relation to the comparative complexity of cases.

### RECOMMENDATION 4.7

*To ensure that the ATO appropriately resources its compliance activities in relation to HWIs, S4 and Wealthy Australian taxpayers, the ATO should:*

- a. identify and fill gaps in resourcing (such as that identified in its internal report, 'Review of interpretative advice as part of the SM&E pipeline');*
- b. ensure that relevant information on workflows and resourcing is shared within the SME business line;*
- c. based on the increased complexity of this work, reassess the expected workloads of its SME Active Compliance, SME Interpretative Assistance (IA) officers and other ATO officers involved in dispute resolution (such as TCN and litigation);*

---

<sup>65</sup> Ibid, p. 27.

<sup>66</sup> Australian Taxation Office, written communication to the IGT, 23 September 2011.

## RECOMMENDATION 4.7 (CONTINUED)

- d. assess the impacts of this compliance action on other SME business line commitments; and*
- e. sufficiently resource the SME's IA function to appropriately handle the number and complexity of objections being, and expected to be, lodged.*

### ATO response: Agree

We will implement the recommendations of the S&ME commissioned report ('Review of Interpretative Advice as part of the S&ME pipeline) which was prepared for the S&ME Executive in June 2011.

Active Compliance provides a report to Interpretative Advice on the expected workloads and timing of case work which may flow into the Interpretative Advice area.

This report allows Interpretative Advice to better align their resourcing and work priorities with current and expected workloads.

4.57 During the review, the IGT received submissions from ATO staff concerned with aspects of the SME business line, including how the business line handled concerns raised with senior officials. The IGT has considered the issues insofar as they relate to the ATO in its role as a tax administrator. However, some issues related to the ATO in its role as an employer. In this respect, the IGT considered that there were alternative workplace relations mechanisms designed to resolve such concerns.

## CHANGE MANAGEMENT

4.58 The SME Executive recently implemented a number of substantial changes to address approaches in relation to integration, private wealth, the S4 market, WA work, and candidate HWIs' identification.

4.59 Generally, 'integration' within the SME business line refers to the merging of the GC, HWI and WAs areas into one. Senior SME staff explained that the aim is to remove the internal silo stacks of these areas and put them together into one area. The SME business line recognises that there will be many streams of work, but does not intend staff to do work that they are not equipped to deal with. It will be up to the team leaders and regional directors to match the existing capability with the work required to be done in line with the ATO's commitments to Government. The ATO advises that integration occurred in mid-October 2011.

4.60 Submissions from certain ATO staff indicate that it is unclear the extent to which staff understand how the transitions will impact on their work (that is, what their job is and how they are expected to do it).

4.61 In the IGT's view, the SME business line could improve staff understanding of the integration and its impact on the GC, WA and HWI areas.

#### **RECOMMENDATION 4.8**

*The ATO should improve staff understanding of the integration of the General Compliance, Wealthy Australians and HWIs areas and its impact on staff.*

ATO response: Agree

We delivered staff information sessions to all S&ME staff during October and November 2011. These sessions detailed our line priorities, our focus on understanding and managing compliance within our various populations and linking this to the ATO strategic plan. The sessions also covered our use of the RDF, active compliance integration, interpretative assistance and our marketing and education activities.

## CHAPTER 5 — AUDIT CONDUCT, COMMUNICATION AND TAXPAYER ENGAGEMENT

5.1 The manner in which compliance activities are carried out can affect the substantive issues under examination as well as future compliance postures adopted by taxpayers and their advisers.

5.2 The ATO has a number of processes and procedures to help guide its officers in dealing with taxpayers and their advisers in the course of compliance activities. Notwithstanding these processes and procedures, submissions to the review raised a number of concerns with the conduct of compliance activities and the effectiveness of existing escalation processes. Generally, a desire was expressed for increased transparency and awareness of internal ATO processes in this respect.

5.3 In this respect, the ATO's current version of the *Wealthy and wise* booklet sets out the expectations the ATO has of its officers in the conduct of HWI compliance activities. It sets out a range of material useful to HWIs and their advisers, including the issues and characteristics that attract the ATO's attention and how the ATO generally conducts its compliance activities in relation to HWIs.

5.4 During the review the ATO agreed to extend the scope of the booklet to the entire SME market segment. This, in the IGT's view, is a welcome initiative.

5.5 However, notwithstanding the beneficial nature of this document, there are a number of specific areas in which the content of the document could be improved to better set expectations on SME officer conduct. These areas are discussed below and include: escalation processes; opening meetings for compliance activities; allowing tax advisers to be more effective; communicating the commencement and finalisation of compliance activities; having discussions with taxpayers before adverse ATO views are documented in writing; changing the basis for amendments; and changing auditors during compliance activities.

### EXPECTATIONS AND ESCALATION PROCESSES

5.6 In the large business market, the ATO's publication, *Large business and tax compliance* (the 'blue book') sets out the relationship that external parties can expect during ATO compliance activities and related processes, such as escalation processes. Among other things, this set of expectations allows taxpayers to hold ATO officers to account where they do not meet the expectations set out in the ATO's publication.



5.7 In the HWI market, the current version of the ATO's *Wealthy and wise* booklet<sup>67</sup> seeks to provide a similar kind of assistance, but only in a much more generalised fashion.

5.8 A number of submissions to the IGT review claimed that they experienced a level of intimidation and perceived a lack of accountability for ATO officer behaviours in SME and HWI active compliance activities. They did not consider that there was a clear escalation pathway for the compliance activity conduct that caused them concern. They considered that existing escalation processes for the SME market (such as escalating to the team leader and then to ATO complaints) are sometimes ineffective, especially when they concern an auditor's conduct, and that discussing matters with personal contacts within the ATO is generally more effective.

5.9 During the review, the ATO agreed to extend the approach taken in the ATO's blue book to the SME market segment so as to improve the public awareness of the procedural and behavioural conduct that could be expected in the ATO's interaction with HWI and WAs as well as all SME taxpayers. Specifically, the ATO advised:

The current version of the 'Wealthy and Wise' booklet (published in March 2008) will be replaced by a new booklet to reflect an updated and broader view of our approach to managing compliance from a private wealth/private group approach and more broadly across the S&ME market.

The new booklet will provide guidance on our risk assessment and compliance approach to the private group/wealth market along with the broader S&ME segment. It will also provide guidance on our relationships and interactions with taxpayers and advisers, the behaviours we would expect to see from our people, and the procedures we would follow when conducting risk assessment, review and audit activity in the segment.

Like the 'Large business and tax compliance' booklet our expectations of taxpayers and advisors in terms of their tax compliance and their interaction with us during our activities will also be covered.

We see the development of the new booklet as a collaborative and co design process with both taxpayers and advisers in this segment. We will be engaging with a range of external and internal stakeholders in the process of developing the new booklet. We are targeting a publication date of July 2012.

This work provides an opportunity for the ATO to engage with the tax profession and relevant taxpayers to ensure that shared expectations between the ATO and these market segments are fostered in relation to the conduct of compliance activities. It is also an opportunity to develop improved stakeholder perceptions of ATO accountability.<sup>68</sup>

5.10 In the IGT's view, this ATO advice is welcomed as it improves shared expectations on what the SME business line will and will not do during compliance

---

<sup>67</sup> Australian Taxation Office, *Wealthy and wise: a tax guide for Australia's wealthiest people*, Canberra, March 2008.

<sup>68</sup> Australian Taxation Office, written communication to the IGT, 23 September 2011.

activities, the manner in which those activities are conducted and how taxpayers and advisers can hold SME officers to account (such as how matters can be escalated to senior ATO officials for rectification) where they do not meet those expectations. Setting such expectations would go some way to allaying concerns of some in the private sector that, at present, there are no effective means of holding SME officers to account.

## **RECOMMENDATION 5.1**

*In consultation with taxpayers, tax practitioners and their representative bodies, the ATO should replace its 'Wealthy and wise' booklet (published in March 2008) with a new booklet to apply across the SME market segment that more clearly communicates what specific conduct taxpayers and their advisers can expect during compliance activities. This booklet should set clear expectations, including:*

- a. what the ATO will and will not do during compliance activities in the SME market segment (including HWIs and Wealthy Australians);*
- b. the manner in which those activities will be conducted; and*
- c. more effective escalation processes where the ATO's SME officers do not meet those expectations.*

### **ATO response: Agree**

We are currently working on the development of a comprehensive booklet which will focus on the private wealth segment (net wealth over \$5 million) as well as the broader S&ME market (entities with turnover between \$2 million and \$250 million).

The booklet will detail our approach to assessing risk and managing compliance in these market segments. It will also outline the behaviours we would expect to see from taxpayers and advisers in these segments along with the behaviours expected from tax officers when they are dealing with taxpayers and advisers in these segments

In general we support the views in the range of recommendations in this report which are related to the publication of a new booklet.

We have formed a working group of key tax professionals to assist us in the development of the booklet.

The views of this group will be taken into account in finalising the content of the booklet and will be considered in terms of the implementation of the recommendations in this report which relate to the publication of the booklet.

5.11 As indicated above there are a number of issues concerning the setting of expectations of SME officer conduct. The replacement of the *Wealthy and wise* booklet provides an appropriate vehicle to communicate these expectations. As such there are

a number of recommendations that are directed to the content of this booklet. These issues and the recommendations are discussed below.

## OPENING MEETINGS FOR COMPLIANCE ACTIVITIES

5.12 The current version of the *Wealthy and wise* booklet states that at the beginning of an audit the ATO:

Will generally:

... discuss with you or your adviser the risk/issue and the information we propose to seek, including the reasons we are seeking it. The aim of the discussion is to refine our information needs to ensure adequate information is obtained in the shortest possible time. We will seek your views on any concerns, ambiguities or issues of relevance and your assistance to identify other information that would assist in the timely completion of the audit

... discuss with you our information-gathering protocols and expectations, including our timeliness for the provision of information and appropriate resource levels

... take into account your particular circumstances to minimise the inconvenience and cost of our enquiries

... Hold preliminary audit interview

At the interview we will:

- provide you with a copy of the audit plan;
- discuss the audit scope, the periods under audit and the expected completion date;
- discuss the information gathering process;
- discuss any Tax Office guidelines relevant to the issues and years to be audited, including procedures in relation to voluntary disclosures;
- Outline facilities and assistance we may require; and
- give you contact details for a senior officer in case you wish to raise any concerns during the audit.<sup>69</sup>

5.13 In the IGT's view, the above should be expanded in a number of respects, including covering risk reviews and audits of S4 taxpayers and WAs.

---

<sup>69</sup> Australian Taxation Office, *Wealthy and wise: a tax guide for Australia's wealthiest people*, Canberra, March 2008, pp. 32, 42.

## RECOMMENDATION 5.2

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that at the outset of any compliance activity ATO officers will meet with the taxpayer and/or their representatives. The purpose of this meeting will include the following:*

- a. identify the areas to be reviewed or audited;*
- b. identify the information that the ATO is seeking and whether there are alternative forms of the information that would fulfil ATO purposes and be of reduced compliance burden to the taxpayer;*
- c. agree on the timeframes for the compliance activity and deadlines for key milestones in that activity; and*
- d. commit to the aim of 'no surprises' and the means to achieve that aim, such as periodic ongoing communication, preferred communication channels and escalation processes for any concerns arising during the audit.*

ATO response: Agree

## ALLOWING TAX ADVISERS TO BE MORE EFFECTIVE

5.14 Under the SME business line's current compliance activity procedures, there is no requirement for SME officers to allow tax advisers time to internally review their clients' affairs before reviews or audits commence.

5.15 In the IGT's view, affording tax advisers an opportunity to internally review clients' affairs and make voluntary disclosures before the ATO commences information gathering could substantially reduce direct SME officer time on reviews and audits and reduce taxpayers' costs.

5.16 Separately, under the SME business line's population strategy, the SME business line is exploring pre-activity relationship development with HWIs' tax advisers so that case plans are discussed with the tax adviser prior to any audit activity being started. This initiative is similar to the LBI business line's relationship management process.

5.17 In the IGT's view, discussing and developing compliance activity case plans with the representatives of the taxpayer before any activity commences would improve taxpayer engagement and access to the relevant information needed. If there were to be circumstances in which this opportunity was not to be afforded (such as appropriately commenced covert audits involving organised criminal activity), this should be explicitly stated in the relevant publication.

### RECOMMENDATION 5.3

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that ATO officers will discuss and develop compliance activity case plans with the taxpayer's representatives before any activity commences. If there are circumstances in which this opportunity was not to be afforded, these circumstances will be explicitly stated also.*

ATO reponse: Agree

### DISCUSSION WITH TAXPAYERS BEFORE VIEWS ARE DOCUMENTED IN WRITING

5.18 A number of submissions to the IGT review commented that SME officers appear committed to a course of action once the ATO position is in writing, even if in draft form, such as draft position papers. The submissions comment that they perceive entrenched views were only objectively re-assessed when signals that the ATO view may not be correct were raised with more senior ATO officials. This occurred after considerable delay and associated costs being incurred.

5.19 Some submissions observed quick and streamlined resolution of issues when the Facts and Evidence Worksheet (a compliance officer's internal working document) was disclosed by the officer and the practitioner was afforded an opportunity to comment on it in discussion with relevant technical officers. The IGT has also observed in other areas that this practice of disclosing similar types of worksheets were effective in quickly and effectively resolving some of the ATO's most complex compliance cases.

5.20 According to the current version of the *Wealthy and wise* booklet, there is no requirement for an officer to discuss the issues with the tax adviser before a position paper is communicated—for example, under a HWI compliance activity, discussions are guaranteed only after issue of the draft finalisation letter (for review) and position paper (for audit).

5.21 There are indications that some SME officers may consider such discussion with taxpayers unnecessary and would provide opportunities for delay in completing compliance activities.

5.22 In the IGT's view, requiring officers to discuss potential views with taxpayers and their advisers before drafting a position paper provides a means to efficiently and effectively narrow the issues in dispute, so long as that discussion is focussed. Sharing properly prepared Facts and Evidence Worksheets with taxpayers and their advisers provides the means for focusing those discussions. There may be a view that this action may provide additional opportunities for some taxpayers to delay the compliance processes. However, this view should be balanced against the downstream impacts for not doing so, such as increased timeframes and intensity of disputes during the objections and litigation stages.

## RECOMMENDATION 5.4

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that ATO officers, based on the relevant facts and evidence worksheet which they have prepared, will discuss potential views with taxpayers and their advisers before drafting a position paper that may have adverse impact on them.*

ATO response: Partially agree

We will include in the new booklet commentary on the nature of our engagement with taxpayers in the course of us preparing position papers and throughout the course of the audit.

We will continue to use the facts and evidence worksheet in the course of developing our view.

It remains a key component in the process of developing a position paper.

We will discuss key issues with taxpayers in the course of developing our position paper.

## CHANGING THE BASIS FOR AMENDMENTS

5.23 In some cases, the ATO reasons for amending a taxpayer's liability may change after the assessments are amended (such as in objection decisions or litigation). There is no requirement for SME officers to notify taxpayers for the reasons of this change – for example, why the views ultimately relied upon were not raised during audit.

5.24 Some submissions received from certain ATO staff indicate that they are aware of a number of cases where the ATO has raised an assessment in circumstances where the period for review was close to running out and an ATO position was still not fully formulated. In those cases, the SME business line issued amendments and subsequently worked to develop the position in the ATO's response to the objection and litigation.

5.25 An internal ATO report also commented that SME objection officers observed some audits reaching objections in a 'poor state' due to, amongst other reasons:

Lack of properly considered position – protective assessments due to time constraints and assessment issued while audit still underway.<sup>70</sup>

5.26 Some private sector submissions claim that these occurrences are not uncommon and that they burden the taxpayer with unnecessary costs and shift the

---

<sup>70</sup> 'Review of interpretative advice as part of the SM&E pipeline', a report commissioned by and prepared for the ATO's SME Executive, June 2011, p. 23.

identification and testing of risk hypotheses into the formal and more costly Part IVC (of the *Taxation Administration Act 1953*) dispute resolution process.

5.27 The IGT understands that there may be circumstances in compliance activities where there is a need to take protective action and there is not enough time to formulate a concluded ATO position, such as where the taxpayer has deliberately avoided contact with the ATO over a period of years despite repeated and numerous attempts by the ATO to establish contact. These circumstances, however, should be rare. Where these circumstances arise, the ATO should take fair and reasonable action to minimise the costs imposed on that taxpayer by reason of changing the ATO position during the dispute resolution process. This action should include, at the least, communicating the reasons why the view was not formulated earlier, GIC remission and a concessional approach to penalty remission.

### **RECOMMENDATION 5.5**

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that where the ATO's reasons for amending a taxpayer's liability change after assessments change (such as during the consideration of objections or litigation), the ATO will take fair and reasonable action to minimise the costs imposed on that taxpayer by reason of that change, including:*

- a. communicating the reasons why the new ATO position was not formulated earlier;*
- b. GIC remission; and*
- c. a concessional approach to penalty remission.*

ATO response: Agree

### **CHANGING AUDITORS DURING COMPLIANCE ACTIVITIES**

5.28 Submissions to the IGT indicate that concerns with the change of SME officers during compliance activities. They cite increased costs in bringing new SME officers up-to-date where those officers are not aware of the information already provided or have not sought to understand that information before engaging with the taxpayer or their adviser.

5.29 In the IGT's view, the ATO should take steps to minimise taxpayers' costs arising from changing staff during SME compliance activities.



## RECOMMENDATION 5.6

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that the ATO will minimise taxpayers' costs arising from the change of SME officers during compliance activities. This will include, before engaging with the taxpayer or tax adviser the new compliance officer will:*

- a. familiarise themselves with the issues, facts and status of the compliance case; and*
- b. understand the information that has already been provided by the taxpayer and how that relates to the issues in question.*

ATO response: Agree

## COMMUNICATING COMMENCEMENT AND FINALISATION OF COMPLIANCE ACTIVITIES

5.30 The current version of the *Wealthy and wise* booklet states that, among other key events in active compliance activities, officers are to:

- provide a finalisation letter to taxpayers where they decide that no further action is to be taken as a result of a risk review;
- provide a draft finalisation letter for any risks that are intended to be audited; and
- 'generally' notify taxpayers of an intention to audit.

5.31 In 2010, an SME business line's workshop with externals<sup>71</sup> identified 1 of 4 cases where transition from CRR to Specific Audit was not communicated to taxpayers. The later workshop with externals<sup>72</sup> also identified in some of the 8 cases where the transition from review to audit was not communicated to taxpayers.

5.32 In the IGT's view, more could be done to ensure SME officer compliance with existing notification procedures, such as the commencement and finalisation of compliance activities. Further, the ATO could more clearly set expectations about such notification by clearly stating when officers are to provide such notification.

---

71 The SME Community Involvement workshop (a process through which the ATO identifies areas for improvement), March 2010.

72 The SME Community Involvement workshop, August 2010



## **RECOMMENDATION 5.7**

*In relation to existing notification procedures concerning the commencement and finalisation of compliance activities, the SME business line should:*

- a. in addition to existing quality assurance measures, ensure that its officers comply with these procedures; and*
- b. more clearly set expectations about such notification by clearly and publicly stating when officers are to provide such notification.*

**ATO response: Agree**

We will issue clear instructions to staff around advising taxpayers of the commencement and finalisation of compliance activities.

## CHAPTER 6 — INFORMATION GATHERING

6.1 The ATO generally seeks to take a staged approach to information gathering. In the ATO compliance environment, the approach is usually to commence information gathering to assess whether there are tax risks arising from a taxpayer's self-assessment of their tax obligations (a risk review). It is expected that risk reviews involve a lower intensity of information gathering compared to that of an audit. In relation to HWI and S4 cases, the ATO seeks to impose a lower level of burden of information gathering initially by scoping risks in a Preliminary Risk Review (PRR) before undertaking a Comprehensive Risk Review (CRR) or audit. The ATO also has a general policy of asking for information informally, rather than using formal powers at first instance, such as those under section 264 of the *Income Tax Assessment Act 1936*.

6.2 The SME business line also uses expanded returns for those HWIs that it considers exhibit a higher risk rating. The ATO may also use expanded returns for a number of years following adverse compliance action to assure itself that the HWI is correctly complying with the tax laws.

6.3 The IGT has observed that some of the stakeholders' experiences have been very mixed in relation to information gathering in compliance activities of S4, HWI and WAs. Stakeholders have conveyed a need for greater ATO communication and engagement on the overall information gathering process along with better targeting of requests and minimising the time taken for ATO responses and related follow up.

6.4 During the IGT's review the ATO advised:

S&ME will implement a new centralised case preparation and selection process which is designed to utilise more of our new automated data collection and collation processes.

The new process will provide our active compliance staff with a much richer picture of the taxpayer and the risks associated with that taxpayer along with all the relevant information the ATO holds on that taxpayer prior to us having any contact with the taxpayer or their advisor.

This process will minimise the need to contact taxpayers or advisers for the basic information we might need prior to commencing a review or audit.

... While further information requests will remain part of the review and audit process S&ME will review its procedures related to seeking and managing further information requests to ensure that they support full engagement with the taxpayer or advisers in relation to the nature, extent and timing of such requests.<sup>73</sup>

6.5 In the IGT's view, better management of the ATO's contact with taxpayers and their advisers to obtain basic information should go some way to minimising compliance costs imposed by these types of information requests. The ATO's

---

73 Australian Taxation Office, written communication to the IGT, 23 September 2011.

commitment to engaging taxpayers and their advisers in relation to further information requests also provides an opportunity to manage relationships and improve compliance outcomes and taxpayers' experiences. Further areas for improvement in relation to information gathering activities are identified below.

## **SETTING EXPECTATIONS IN INFORMATION GATHERING**

6.6 The ATO's confidence that its SME business line has correctly assessed risks is directly related to the amount of source information obtained and the depth of risk assessment activities.

6.7 The ATO is in the final stages of risk reviewing all S4 entities, approximately 1400 in number. This market segment predominately comprises private groups and entities, having a lower level of publicly available information than that of larger businesses. This is the first time that the ATO has reviewed this market segment in this manner. It is likely that many of these entities have not previously been the subject of ATO compliance activities and a greater level of information is likely to be required than would otherwise be the case.

6.8 There were also indications that initially there may have been an inconsistent approach to gathering information from S4 taxpayers, particularly in relation to the stage at which financial statements are requested by the ATO and which entities within an S4 group should be targeted.

6.9 Some submissions to the IGT review also observed unfocussed information gathering requests in both reviews and audits. They have cited some examples of requests for information already provided to the ATO. They also observe that the ATO has sometimes made information requests of third parties without informing the taxpayer first, thereby adversely affecting the commercial relationships between taxpayers and third parties.

6.10 As discussed in chapter three, the ATO uses a Facts and Evidence Worksheet to focus compliance officers' attention on technical decision making. However, at present, there is no SME business line requirement to use the Facts and Evidence Worksheet to focus technical thinking and determine the information that should be gathered to test risks. The only requirement is to use the worksheet as the means for recording the facts and evidence of the case.

6.11 During the review the ATO advised that:

We will reissue the instructions and reinforce the requirements to use the Facts and Evidence worksheet in a range of S&ME case work.<sup>74</sup>

6.12 In the IGT's view, the ATO could do more to closely set private sector expectations on what information will be obtained during risk review stages. Additionally, after the risk hypotheses are developed by SME auditors, proper use of

---

<sup>74</sup> Australian Taxation Office communication to the IGT, 23 September 2011.

the Facts and Evidence Worksheet would minimise the incidence of unfocussed information gathering occurring during audits.

## **RECOMMENDATION 6.1**

*The SME business line should require its compliance officers to use the Facts and Evidence Worksheet to determine what information will be asked of a taxpayer in any particular compliance activity.*

### **ATO response: Agree**

The facts and evidence worksheet is required to be used in audit cases. This has been the case since April 2010. We will reinforce this business rule with our staff to ensure its use in all cases.

The worksheet remains a key part of the process for determining and seeking further information during our audit activity.

6.13 As discussed in the previous chapter, the Facts and Evidence Worksheet can also be shared with the taxpayer to focus discussion on technical issues.

## **ASYMMETRIES IN TIMEFRAMES**

6.14 Depending on the type of information requested, the ATO may require taxpayers to provide information within a set time period (generally 28 days) or otherwise as negotiated. However, there is no such similar requirement on the ATO to respond to the taxpayers' requests or responses within set timeframes.

6.15 Some submissions commented that extended delays in the ATO responding to information provided (such as further follow up or discussion of issues arising from the information provided) result in increased costs to advisers and taxpayers by reason of the time taken to re-familiarise themselves with matters and issues. They observed this occurred in various types of compliance activities in relation to various types of taxpayers.

6.16 In the IGT's view, the ATO should better manage and meet private sector expectations around the time periods in which the ATO should review and respond to information provided. Team leaders should also ensure that cases are progressing in a manner that provides taxpayers with adequate time to respond to ATO information requests and minimises the time taken by SME officers to progress and finalise cases.

## RECOMMENDATION 6.2

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that in relation to ATO information requests, the SME business line will:*

- a. clearly state to taxpayers and their advisers the time periods within which the ATO will review and respond to information provided by them; and*
- b. ensure that team leaders are progressing cases in a manner that provides taxpayers with adequate time to respond and minimises the time taken by SME officers to finalise cases.*

ATO response: Agree

## PRIVATE GROUP STRUCTURE QUESTIONNAIRES

6.17 During the initial phase of the IGT's review, a significant number of tax advisers made representations on the SME business line's use of its *Private group structure questionnaires*. They claimed that the questionnaires were unclear in terms of the information requested and time period to which they related. Also the questionnaires asked for information concerning family members and associates, while similar questionnaires were sent to those family members and associates as well, thereby duplicating the information required. They also claimed that after providing the information, long periods of time elapsed before the ATO responded, which in many cases was a further request for information or questions on the information provided.

6.18 The SME business line acknowledges that it did not properly consider staging the issuing of these information requests, particularly in relation to ensuring it had enough resources available to deal with the responses and follow up requests. It now understands that this market segment may not have been exposed to such information requests previously and could have better engaged with these taxpayers before sending out the questionnaires. The SME business line has also undertaken to review the content of the questionnaires with their SME advisory group (an ATO consultative forum comprising private sector SME representatives and senior ATO staff).

6.19 The SME business line has, in more recent times, established a program of structured scrutiny of S4 and WA taxpayers through its S4 risk review, HWI expansion and WA initiatives. The ATO required a greater level of information from these taxpayers (and other related or connected taxpayers) as it did not have detailed knowledge of the broader economic group to which they were related. In many situations this will be the first time that many of these entities have dealt with the ATO on this basis.

6.20 The IGT considers that there is significant scope for improvement in better preparing taxpayers for new information gathering questionnaires and generally better managing the entire process.

### **RECOMMENDATION 6.3**

*The ATO should review, with their SME advisory group, the structure and content of any proposed new (or substantial alterations to existing) information gathering questionnaires.*

**ATO response: Agree**

We work with the S&ME ATPF group to ensure our questionnaires and outbound letters are effective, appropriate and minimum cost to taxpayers.

### **INFORMATION GATHERING INITIATIVES**

6.21 The ATO project, *KPMG Risk Assessment Information Sharing (RAIS) Phase 1*, is aimed at improving information gathering in the S4 market segment, amongst other things. It grew out of KPMG expressing an interest in better understanding the SME business line's risk management process and the risk classification assigned to their clients in the S4 market segment. The ATO considered that an improved understanding would lead to a more accurate assessment of the ATO's risk profiling of the taxpayers and minimise the chance of inappropriate taxpayer risk selection. The SME Executive approved the project outline in September 2009.

6.22 The ATO is also conducting an Annual Compliance Arrangement Lite Project which is based on the large business annual compliance agreements but with a reduced amount of information gathering.

6.23 Other tax advisers have commented favourably about the objectives of these initiatives.

6.24 In the IGT's view there is potential to use the findings from the RAIS project to develop a strategy for improving information gathering and risk assessment through communicating to each taxpayer the risks that the SME business line has identified in relation to that taxpayer.

### **RECOMMENDATION 6.4**

*The ATO should use the findings from the Risk Assessment Information Sharing project to develop improved information gathering and risk assessment and by communicating to each taxpayer the risks that the SME business line has identified in relation to that taxpayer.*

ATO reponse: Agree

We plan to make use of the data and knowledge we gain from the current Risk Assessment Information Sharing (RAIS) pilot to expand this activity to other practitioners and taxpayers in our market where appropriate.



# APPENDIX 1 — TERMS OF REFERENCE AND SUBMISSION GUIDELINES

## BACKGROUND

During the Inspector-General of Taxation's (IGT) work program consultations, representatives of small and medium enterprises (SMEs) and high wealth individuals (HWIs) raised a number of concerns with the Australian Taxation Office's (ATO) review and audit approaches.

These concerns generally related to taxpayers receiving fair and equitable treatment and not being unduly burdened with unnecessary compliance costs stemming from the wide scope of ATO information gathering requests, delays, commercial awareness and conduct of ATO staff and the quality of ATO engagement on technical issues.

Particular concerns were raised on the implications of certain ATO announcements made from late 2008. These announcements explained that as a result of additional funding from the Government<sup>75</sup>, the ATO would:

- expand its compliance activities to risk assess over a 4-year period all businesses with annual turnovers between \$100 million to \$250 million<sup>76</sup>, and follow this work up with more reviews and audits; and
- increase its monitoring, reviews and audits of High Wealth Individuals (HWIs).

The ATO announcements raise a concern that unless certain compliance approaches are improved, this additional ATO compliance focus will significantly increase unnecessary costs and unmanageable workloads for taxpayers as well as creating unnecessary administrative costs for the ATO.

The ATO announcements show that it plans to increase resourcing of its compliance areas to man these additional compliance activities. However, there are concerns that the ATO may not have sufficiently resourced its technical areas (such as the Centres of Expertise and Tax Counsel Network) to adequately deal with the increased workload that these compliance activities may generate for the ATO's Law Sub-Plan.

The Inspector-General now seeks to establish whether there is substantiated evidence of these concerns.

---

75 In the 2008 and 2009 Federal Budgets, the Government allocated an additional \$559 million of funding to the ATO for the purpose of enhancing the ATO's compliance activities and management of known tax risks in relation to the large business and high wealth individual market segments. This additional funding will be provided over the period 2008 to 2013 and is expected to increase Government revenues by \$3.28 billion. Only part of this additional funding relates to the ATO's increased compliance focus on SMEs and HWIs.

76 The ATO previously categorised these businesses as 'large businesses'. However, the ATO has recently re-categorised these businesses as 'small and medium enterprises'.

In investigating these concerns, the IGT will review the relevant ATO files and may interview ATO staff to identify the reasons for the ATO approaches, the steps the ATO took to minimise adverse outcomes for taxpayers and identify potential improvements.

## **Terms of reference**

In accordance with subsection 8(1) of the *Inspector-General of Taxation Act 2003*, the Inspector-General conducts the following review at the direction of the Minister.

*The IGT will review aspects of the ATO's compliance approaches to determine whether compliance activities of SMEs with annual turnovers between \$100 million and \$250 million and HWIs are being handled so as to promote their timely, efficient and fair resolution.*

*The IGT will also identify opportunities for improvement.*

*The review will have a particular focus on the ATO's:*

### **Resourcing**

1. *the extent to which the ATO has resourced its compliance and law sub-plans to deal with the intended increase in compliance activities in relation to these taxpayers, including:*
  - a. *whether the ATO auditors have the appropriate technical skill level and appropriately understand the commercial environment in which the taxpayer operates (such as, the effect that non-tax law has on the relevant industry);*
  - b. *whether the ATO has allocated enough senior technical resources (such as in the Centres of Expertise and Tax Counsel Network) for any increased workloads that its increased compliance focus may generate;*

### **Information gathering**

2. *in light of the limited resources that taxpayers in this market segment may be able to allocate for tax and other regulatory compliance, the extent to which the ATO ensures the exercise of its information gathering powers, both formally (such as, s.264 notices) and informally, is being used appropriately and effectively (such as, the extent to which the ATO targets its information requests, minimises the potential for immaterial or duplicated information requests and explains the reasons for needing such information);*
3. *the extent to which asymmetry in timeframes for the ATO's and taxpayers' responses impact on taxpayers' costs – for example, the time periods that taxpayers have to respond to ATO information requests and the time periods that the ATO may take in considering and following up on those taxpayer responses;*

### **Compliance decisions**

4. *the extent to which the ATO ensures that its initial compliance decisions are accurate, including:*
  - a. *whether initial compliance decisions (such as penalties and primary tax liabilities) appropriately consider the evidentiary, specialist tax technical and commercial (for example, valuations) issues, appropriately consider the relevant burden of proof, and*

*minimise perceptions that they are used to establish an unfair advantage during negotiations;*

*b. whether allegations of evasion have an accurate evidentiary basis and are not used to audit or review issues which would otherwise be out of time in a self-assessment regime or for any other purpose;*

*5. on the same material facts, the extent to which ATO provides reasons for changes in views expressed throughout the audit and dispute process (for example, where the views expressed in the objection and/or appeal stage change from the initial audit stage) and minimises the impact on taxpayers' compliance costs where those views change;*

### **Technical issue management**

*6. whether the ATO's conduct of compliance activities promote an appropriate and timely narrowing and/or resolution of issues in dispute, including:*

*a. whether there is sufficient initial prioritisation and scoping of issues for examination in the compliance activity to ensure that the highest risks to the tax system are examined and unnecessary compliance costs minimised;*

*b. the extent to which the conduct of compliance activities promote a timely understanding of the strengths and weaknesses of each parties' case (such as whether the ATO provides sufficient time for taxpayers to test the factual and evidentiary basis for proposed ATO compliance decisions or position papers) and makes timely decisions on the appropriate resolution of cases;*

*c. ensuring that ATO auditors follow the ATO's internal technical decision making processes (such as, applying precedential ATO views and citing their sources);*

*d. whether the ATO ensures that there is no inappropriate resistance to engaging in dialogue over technical issues (such as face-to-face access to technical decision-makers or technical advisers);*

### **Project management and compliance activity conduct**

*7. the extent to which the ATO ensures sufficient project management of compliance activities and appropriate conduct in compliance activities, including:*

*a. whether project plans are appropriately developed (such as providing an opportunity to comment on expected timeframes and milestones), communicated to taxpayers (such as the initial project plan, the progress and finalisation of the compliance activity), monitored and complied with;*

*b. the extent to which taxpayers are negatively impacted by relevant ATO staff being located in different geographical location or changes in ATO audit personnel;*

*c. the extent to which the ATO makes appropriate and effective use of taxpayers' advisers in the management of the compliance activity;*

*d. the extent to which the ATO clearly and consistently communicates the commencement of the compliance activities (such as the when an 'audit' starts for taxpayer voluntary disclosure purposes and whether there is a consistent ATO approach to 'full and true disclosure') and the finalisation of those activities;*

*e. whether the ATO appropriately deals with claims of client legal privilege (or legal professional privilege) and the accountants' concession; and*

*f. whether ATO practices facilitate clear accountability, and a clear escalation pathway, for compliance activity conduct/practices/behaviours that cause taxpayer concern.*

In connection with the above terms of reference, we are seeking taxpayer submissions which detail accounts of SME and HWI experiences in dealing with ATO compliance activities, such as audits and risk review products. This would greatly assist us to identify potential systemic issues and allow us to examine these more efficiently and effectively.

We envisage that, broadly, your submission will be divided into two parts: a detailed account of your experience with ATO compliance activities; and, any opportunities to improve ATO compliance activities.

Specifically, it is important to provide a detailed account of specific ATO practices and behaviours that, in your view, impact upon the timely, efficient and effective resolution of an audit or risk review. Additionally, the IGT is also seeking examples of positive ATO practices and behaviours that contributed to the timely resolution of an audit or risk review.

As far possible, these practices should address the terms of reference above.

In investigating the ATO's audit and risk review practices and related behaviours, it would be useful to provide a time line of events outlining your key interactions with the ATO including information requests, key meetings, the issuing of position papers and ATO amended assessments (if relevant).

Any adverse or detrimental impacts of the ATO's audit and risk review practices and behaviours should then be set out and, if possible, the costs quantified. These might include unanticipated tax liabilities raised in amended assessments (including tax, penalties and interest) for prior years, increased compliance costs in dealing with the ATO directly during the audit or increased ongoing compliance costs thereafter and potential restructuring of significant commercial arrangements.

Your submission should list alternative actions, practices or behaviours which, in your view, could minimise the adverse effects of ATO compliance activities.

## Lodgement of submissions

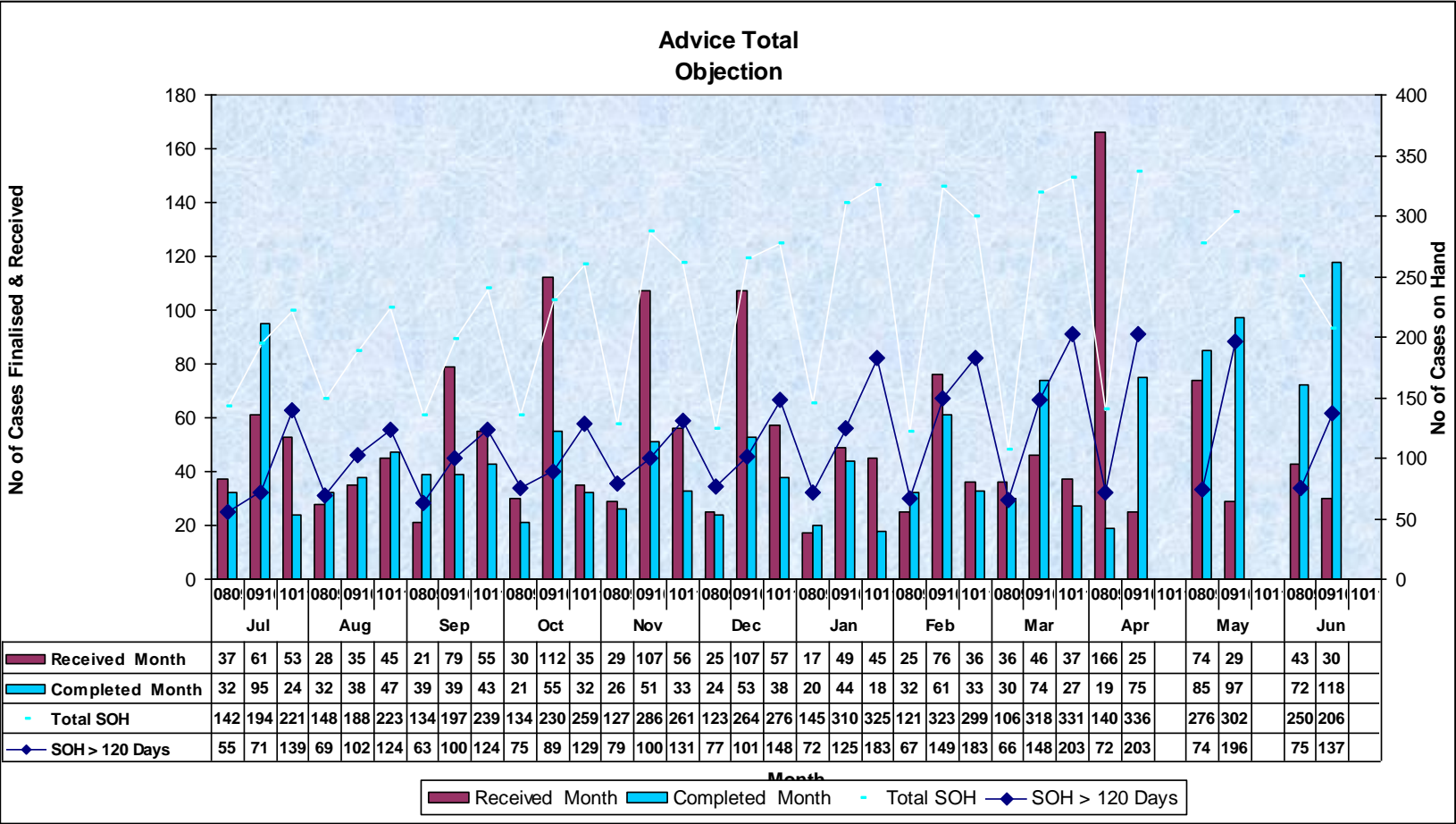
The closing date for submissions is 31 May 2010. Submissions can be sent by:

Post to:           Inspector-General of Taxation  
                      GPO Box 551  
                      SYDNEY NSW 2001  
Email to:          sme@igt.gov.au

## Confidentiality

Submissions provided to the IGT are in strict confidence (unless you specify otherwise). This means that the identity of the taxpayer, the identity of the adviser and any information contained in such submissions will not be made available to any other person, including the ATO. Sections 23, 26 and 37 of the IGT Act 2003 safeguard the confidentiality and secrecy of such information provided to the IGT — for example, the IGT cannot disclose the information as a result of an FOI request, or as a result of a court order generally. Furthermore, if such information is the subject of client legal privilege (or legal professional privilege), disclosing that information to the IGT will not result in a waiver of that privilege.

APPENDIX 2 – HWI OBJECTIONS WORKLOADS



## APPENDIX 3 — ATO-IDENTIFIED AREAS FOR IMPROVEMENT



**Australian Government**  
**Australian Taxation Office**

INTERNAL	OFFICE MINUTE	23/09/2011	<b>IN CONFIDENCE</b>
SEGMENT	FORMAT	ISSUE DATE	CLASSIFICATION

### OFFICE MINUTE

FILE  
REF:

TO:	The Inspector General of Taxation		
COPIES TO:	Acting Second Commissioner Compliance, Actg Assistant Commissioner, Corporate Relations		
YOUR REFERENCE:			
FROM:	Acting Deputy Commissioner		
BUSINESS LINE:	Small & Medium Enterprises	SECTION:	Active Compliance
CONTACT OFFICER:		CONTACT PHONE:	
ISSUE DATE:	23 September 2011	RESPONSE DATE:	
SUBJECT:	IGT Review into High Wealth Individuals And S&ME Compliance Activities		

In response to the IGT's preliminary views on areas for improvement and our discussions with the review's working group the ATO has identified the following areas for improvement for active compliance activities in the HWI and S&ME market.

#### 1. Replacement of Wealthy and Wise booklet

The current version of the 'Wealthy and Wise' booklet (published in March 2008) will be replaced by a new booklet to reflect an updated and broader view of our approach to



managing compliance from a private wealth/private group approach and more broadly across the S&ME market.

The new booklet will provide guidance on our risk assessment and compliance approach to the private group/wealth market along with the broader S&ME segment. It will also provide guidance on our relationships and interactions with taxpayers and advisers, the behaviours we would expect to see from our people, and the procedures we would follow when conducting risk assessment, review and audit activity in the segment.

Like the 'Large business and tax compliance' booklet our expectations of taxpayers and advisers in terms of their tax compliance and their interaction with us during our activities will also be covered.

We see the development of the new booklet as a collaborative and co design process with both taxpayers and advisers in this segment. We will be engaging with a range of external and internal stakeholders in the process of developing the new booklet. We are targeting a publication date of July 2012.

## **2. Centralised Case Selection and Preparation**

S&ME will implement a new centralised case preparation and selection process which is designed to utilise more of our new automated data collection and collation processes.

The new process will provide our active compliance staff with a much richer picture of the taxpayer and the risks associated with that taxpayer along with all the relevant information the ATO holds on that taxpayer prior to us having any contact with the taxpayer or their advisor.

This process will minimise the need to contact taxpayers or advisers for the basic information we might need prior to commencing a review or audit.

We will design and build a '*complexity measure and indicator*' into our case selection process to enable us to better understand the nature of case work we plan to undertake. The indicator will also provide us with a better basis for planning our resource needs and allocation of the correct resources to match the case work. We plan to have this in place for the 2012/13 year.

## **3. Information requests**

While further information requests will remain part of the review and audit process S&ME will review its procedures related to seeking and managing further information requests to ensure that they support full engagement with the taxpayer or advisers in relation to the nature, extent and timing of such requests.

## **4. Active Case Management**

S&ME will undertake the following activities to improve our case/project management of active compliance cases:

We will participate in the upcoming cross sub plan roll out of training designed to improve active case management of review and audit cases. This will include a 1 day training session for all staff to be rolled out over the balance of 2011/12.

Outline in the new 'Wealthy and Wise booklet' our focus on and processes around review and audit case/project management

We will upgrade our routine reporting to include 'milestone' reporting of review and audit cases.

For audit cases we will, subject to agreement from the taxpayer and adviser, have the team leader of the audit officer involved in the initial audit interview. The team leader (generally and EL 2 officer) will be initial escalation point for the taxpayer or adviser if there are issues which cannot be resolved with the audit officer. This initiative will be part of our process by March 2012.

In addition to the inclusion of the team leader at the initial audit interview we will also be looking for more opportunities to engage face to face with taxpayers and their advisers. This will allow us to more effectively clarify issues, resolve disputes or misunderstandings and to assist in finalising cases more quickly and effectively. While this activity occurs in many cases now we are looking to expand it as a key part of our audit processes and add to the opportunity it provides to get better technical outcomes and more efficient timeframes for case work. This focus will be built into our processes by the end of the 2011/12 year.

## **5. Collective capability model and ongoing capability build**

S&ME we will continue to use the S&ME capability snapshot data, our learning pathway information, the new corporate Learning & Development capability processes and our team leaders and our senior technical leaders to identify and attend to our skilling and development needs.

We expect to see a larger rollout of skilling opportunities in 2011/12 than was the case in 2010/11 as the corporate Learning & Development processes bed down. We will ensure we take advantage of this by continuing to target our skilling needs and access the skilling and development we need to ensure our work force a capability continues to improve.

We will continue to build our capability based on the ATO model of collective capability. This means we will make regular use of senior technical specialists such as our Senior Technical Leadership team, our SES level case leadership team, our CoE's and TCN to provide support and assistance to case officers as required to resolve technical issues and progress case work.

The upcoming (October 2011) integration of our active compliance workforce's from high wealth individuals (HWI), general compliance and wealthy Australians (WA) will provide us with further opportunities to enhance capability as we will have EL2s leading each of the active compliance teams and a mix of skilled and experienced staff from HWI and general compliance in each team.

Our new 'Wealthy and Wise booklet' will provide a picture of how we use the collective capability model in practice.

We also see our intention to do more face to face work with adviser and taxpayers as providing us with opportunities to improve our capability in resolving technical issues and finalising cases more efficiently.

S&ME will pilot of the 'Transforming Tax Technical Decision Making' project (TTTDM) which is beginning in a September 2011. The program is designed to ensure that specialist technical resources from areas such as CoE s and TCN are involved in and providing advice and assistance on case work early in the life of a review or audit case. This pilot will include having these specialist staff involved in taxpayer interviews and discussions where necessary.

## **6. General Process Improvements.**

We will reissue the instructions and reinforce the requirements to use the Facts and Evidence worksheet in a range of S&ME case work.

We will be taking part in the upcoming Compliance sub plan dispute review processes and will implement any recommendations relevant to S&ME active compliance work which flow from that review.

We are currently working on an improved reporting interface with the Interpretative Assistance area. This will ensure we can track audit cases which proceed to an objection and thereby undertake ongoing analysis and review of the issues which are being dealt with in objection cases. We expect this work will be completed by March 2012.

Please contact [name deleted] if you require any further information on the matters detailed above.

Actg Deputy Commissioner  
Small and Medium Enterprises

## **APPENDIX 4 — CHARACTERISTICS OF EXPERT COMPLIANCE OFFICERS: EXTRACT FROM INSIDE STORY'S REPORT**

A.4.1 In July 2010, Inside Story presented its report, *S&ME Compliance Officer Research*, to the SME business line. The report identified the characteristics of expert compliance officers in five core areas and created an 'Expertise Assessment Tool' from these areas:

### **1. Strategic thinking**

1.1 Convergent thinking—Can distil a large volume of information down to core issues

1.2 Investigative ability (Divergent thinking)—Identifies critical information sources and asks a range of questions to uncover valuable information

1.3 Critical thinking—Seeks to verify identified information, close gaps and resolve discrepancies

1.4 Diagnostic ability—Explores context and relationships between individuals and between individuals and companies to identify beneficiaries of transactions and deals. Seeks to identify path of money and other benefits.

1.5 Recognises links between interconnected issues—Can recognise & identify patterns in information/data/facts bringing multiple elements together

1.6 Focuses strategically—Understands ATO objectives and prioritises work accordingly taking into consideration whether cases and individual risks are material, worth pursuing and pose a reputation risk to ATO

### **2. Draws from previous experience**

2.1 Interprets taxpayer motivations—Able to identify potential taxpayer motivations from case facts and information

2.2 Applies knowledge of an industry—Applies knowledge or actively seeks out to inform themselves about characteristics of an industry to help interpret facts on a current case

### **3. Confidence**

3.1 Displays confidence—Expresses confidence in moving case forward, knowing what steps to take next, consulting others. Able to maintain momentum on case when faced with uncertainty

#### 4. Productive working relationships

4.1 Able to establish rapport and build relationships – Establishes rapport with taxpayers, agents and other representatives

4.2 Seeks cooperative solutions and avoids confrontation – Seeks cooperative agreement on actions and avoids confrontation,

4.3 Communicates process and keeps taxpayer informed of progress – Communicates process and keeps taxpayer informed of progress. Willingness to communicate.

4.4 Personal integrity – Recognises importance of and deals with taxpayers and their representatives transparently and honestly

#### 5. Negotiation skills

5.1 Effectively overcomes delaying tactics – Recognises delaying tactics used by taxpayers and agents and employs effective response

5.2 Able to effectively communicate ATO position in adversarial situations – Able to deal with conflict and communicate ATO position without becoming judgmental. Resilience in adversarial situations – able to remain focused on objectives and not become intimidated

5.3 Judicious use of formal powers – Uses formal powers as a last resort only when diplomatic negotiations have been unsuccessful<sup>77</sup>

---

<sup>77</sup> 'S&ME Compliance Officer Research', a report commissioned by and prepared for the SME Executive, July 2010.

## APPENDIX 5 — ATO RESPONSE



Australian Government  
Australian Taxation Office

SECOND COMMISSIONER OF TAXATION

Mr Ali Noroozi  
Inspector-General of Taxation  
GPO Box 551  
SYDNEY NSW 2001

Dear Ali,

**RE: Review into the ATO's compliance approaches to small and medium enterprises with annual turnovers between \$100 million and \$250 million and high wealth individuals**

Thank you for your letter dated 4 November 2011 and the opportunity to provide comments on your final draft report on the *Review into the ATO's compliance approaches to small and medium enterprises with annual turnovers between \$100 million and \$250 million and high wealth individuals*.

### **Acknowledgements**

I would like to thank you for the collaborative manner in which you have conducted this review. Our involvement with the working party of key practitioners who represent many of the taxpayers in the two market segments which were the focus of the review has enabled us to better understand taxpayer perceptions and some of the issues which are relevant in these market segments.

### **General observations**

I am pleased to note that while you have made a range of recommendations in the report you have also acknowledged that we have been actively working to improve our interaction with taxpayers in these markets and that we have a range of activities underway which will build on our technical capability and assist us to manage compliance in these market segments.

I am also encouraged to see that several of your recommendations are designed to support us in the work we have been doing over the last year or so to enhance a number of our existing processes and practices to ensure we have better outcomes for taxpayers and their advisers and for the ATO.

We are always striving to refine and improve our practices, processes and interactions with taxpayers and advisers. We are also trying to continuously improve the capability of our staff. A number of your recommendations will help us make further improvements which build on our existing staff capability and skilling activities.

PO BOX 900 CIVIC SQUARE ACT 2608 AUSTRALIA  
ADDRESS

+61 (0)2 6216 1111  
TELEPHONE

+61 (0)2 6216 2743  
FACSIMILE

There are a number of recommendations which relate to the work we have underway to replace the "Wealthy and Wise" booklet.

We are developing a comprehensive booklet which will focus on our processes to assess risk, manage compliance and interact with taxpayers and advisers in the private wealth segment, including all taxpayers with net wealth of \$5m or more and entities in the broader small and medium enterprises (S&ME) market with turnover of between \$2m and \$250m.

It will also detail the behaviours we expect to see from taxpayers and advisers in these market segments and also the behaviours we expect from tax officers who are dealing with taxpayers and advisers in these segments.

We have established a reference group of key stakeholders who will work with us to develop the new booklet.

The input and advice from the reference group will help us shape the final product and will be an important part of what we put in place to respond to the recommendations in your report which are dependent on the publication of the new booklet.

**ATO Response to Inspector –General's recommendations**

Our responses to your specific recommendations are at *Attachment 1*. I understand that you will include these under the relevant recommendation in your final report.


In summary, of your 41 recommendations we agree with 38 in full and 2 in part. There is 1 recommendation where we do not agree.

In keeping with the focus of the review, where we have agreed to recommendations we do so in respect of the policy, practices and priorities of the S&ME business line, in particular those related to the two market segments which were the focus of your review.

Thank you again for the opportunity to comment on your report on this review.

If you require further information, please contact Gary Andrews, Assistant Deputy Commissioner S&ME Active Compliance.

Yours sincerely



Bruce Quigley  
Second Commissioner  
Australian Taxation Office

Date: 8 December 2011

[To minimise space, the appendix to the ATO's response has not been reproduced here, but has been inserted into the text of this report underneath each of the recommendations to which that text relates.]



## LIST OF RECOMMENDATIONS

### RECOMMENDATION 2.1

*When selecting SME (including S4, HWI and Wealthy Australian) cases for compliance activity, the ATO should determine the overall complexity for the cases and resource those cases accordingly.*

ATO response: Agree

### RECOMMENDATION 2.2

*The ATO should improve understanding of the roles, responsibilities and accountabilities of the different staff involved in the end to end process of SME cases:*

- a. by ensuring clear guidelines on the roles and responsibilities of key ATO stakeholders in the end to end SME case process and the priority associated with them are available; and b. including in those guidelines, the specific roles, responsibilities and accountabilities of:*
  - i. SME officers, such as risk officers, case officers, advice officers, objection officers, Senior Technical Leadership officers, case leaders, senior management officers; and*
  - ii. non SME officers, such as COE and TCN officers.*

ATO response: Agree

### RECOMMENDATION 2.3

*To strengthen and better match individual SME business line staff capability for specific cases, the ATO should:*

- a. obtain and maintain a formal footprint of each officer's training and experience to identify gaps when compared to the expected knowledge, skills and experience;*
- b. ensure all SME compliance, interpretative assistance and technical officers have a current learning and development plan that includes skills and knowledge development contributing to the delivery of business outcomes; and*

## **RECOMMENDATION 2.3 (CONTINUED)**

- c. allocate work to officers according to their footprint and their learning and development plan.*

ATO response: Agree

## **RECOMMENDATION 2.4**

*The ATO should involve Senior Technical Leadership (STL) officers in resolving technical issues on the basis of the STL officer's area of speciality or expertise.*

ATO response: Agree

## **RECOMMENDATION 2.5**

*To improve the Senior Technical Leadership's (STL) contribution to the SME business line's objectives, the ATO should:*

- a. ensure the STL engages with both Active Compliance and Interpretative Assistance officers, in particular objection officers; and*
- b. involve the STL in the SME Executive's planning for resources and capability development.*

ATO response: Agree

## **RECOMMENDATION 2.6**

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), the role, responsibilities and accountability of the case leadership area should be clearly explained.*

ATO response: Agree

## **RECOMMENDATION 2.7**

*With the aim of developing highly capable SME compliance officers, the ATO should refine its approaches to recruiting and developing its compliance officers by using the Expertise Assessment Tool developed by Inside Story to:*

- a. identify development needs across the SME business line;*

- b. align recruitment and selection criteria with the identified characteristics of 'expert' compliance officers;*
- c. align learning and development programs more closely with the identified characteristics;*
- d. improve on the job training and mentoring; and*
- e. measure the capability development of compliance officers.*

ATO response: Agree

## **RECOMMENDATION 2.8**

*The ATO should facilitate a degree of SME compliance officer specialisation by taxpayer type or industry to better equip them for conducting compliance activities and become better acquainted with the common arrangements of taxpayer types and industries.*

ATO response: Agree

## **RECOMMENDATION 2.9**

*In balancing the need for more capable staff to deal with areas of higher risk and consequence with the need of the SME business line to retain enough of its workforce capability, the ATO should ensure that:*

- a. the LBI business line recruits staff from all business lines including the SME business line; and*
- b. the SME business line recruits capable staff from all areas including the LBI business line, COE and TCN.*

ATO response: Agree

## **RECOMMENDATION 2.10**

*The SME business line should conduct exit interviews for staff leaving to other areas of the ATO irrespective of the reason why a staff member is moving.*

ATO response: Agree

## **RECOMMENDATION 2.11**

*To address SME staff concerns in relation to their work, sufficiently senior ATO staff, who are not the subject of the concerns, should:*

- a. conduct open and frank consultation with the relevant staff;*
- b. seek to understand the concerns and their underlying causes;*
- c. communicate consideration of those concerns including what action will be taken; and*
- d. periodically communicate the status of the remedial action.*

**ATO response: Agree**

## **RECOMMENDATION 2.12**

*In the SME business line recruitment processes, the ATO should emphasise the attractive aspects of the work of this business line such as its complexity, variety and development opportunities.*

**ATO response: Disagree**

## **RECOMMENDATION 2.13**

*The SME business line should take action to retain staff, including establishing a clearer career pathway for existing staff to progress along and deal with more complex work.*

**ATO response: Agree**

## **RECOMMENDATION 2.14**

*With the aim of improving SME business line understanding of commercial and business issues, the ATO should:*

- a. develop programs that provide SME officers with a strong understanding of the business environment and related decision making in taxpayer or industry groups that are the subject of compliance action – such programs should be developed by drawing on:
  - i. input from key tax professional and industry stakeholders;*
  - ii. expertise of Senior Tax Counsel personnel, ATO executive management and external experts;*
  - iii. complaints relating to potential shortfalls in officer training or capability; and**

- b. ensure that before SME officers review/audit taxpayers within a particular industry these officers should have completed, or be accompanied by an officer who has completed, the relevant program of the type outlined in 'a.' above.*

ATO response: Agree

## **RECOMMENDATION 2.15**

*In seeking to improve SME business line staff training, the ATO should:*

- a. provide a broader range of ways to deliver training so that officers have access to information when needed, including a resource library training suite;*
- b. in relation to the external training provided, capture that training in a way that allows it to be disseminated more broadly than those who did not attend and to be reviewed by those that did attend; and*
- c. engage tax practitioners, academics, and business and client management experts to deliver training on a regular basis.*

ATO response: Agree

## **RECOMMENDATION 2.16**

*The ATO should continue measuring the performance indicators for the effectiveness of its training and development activities.*

ATO response: Agree

## **RECOMMENDATION 2.17**

*With the aim of improving the assessment of staff capability development effectiveness measures, the ATO should:*

- a. routinely and systematically capture external views on staff capability as a factor in assessing capability development effectiveness measures;*
- b. take more proactive measures (other than the Staff Professionalism Survey and Client Feedback Questionnaires) to obtain and understand external stakeholders' perceptions of SME officers' capability (such as conducting key client visits); and*
- c. work with private sector stakeholders to improve SME officers' ability to understand their needs and demonstrate sufficient understanding of the relevant issues.*

ATO response: Agree

### **RECOMMENDATION 3.1**

*If the ATO wishes to expand the scope of a compliance activity to encompass issues that were not identified at the point of case selection, then it should only do so after subjecting the issues to an appropriate approval process such as business case approval or risk review. This is designed to ensure that the compliance activity is warranted and that overall compliance costs are minimised.*

ATO response: Agree

### **RECOMMENDATION 3.2**

*The ATO should:*

- a. improve its initial compliance decision making capability to ensure sustainable decisions are made in the first instance; and*
- b. identify the reasons for initial compliance decisions not being upheld on review and take action to address those reasons.*

ATO response: Agree

### **RECOMMENDATION 3.3**

*To improve internal processes dealing with suspicions of evasion, the ATO should:*

- a. ensure that any suggestions of evasion are internally reviewed by senior officers before they are communicated to taxpayers and/or used as a reason to investigate matters; and*
- b. in the event evasion is considered a risk by those senior officers, the case should be referred to the sme technical panel for further action and the taxpayer be notified of this action.*

ATO response: Agree

### **RECOMMENDATION 3.4**

*To improve the evidentiary basis for compliance decisions, the ATO should require SME officers to use the Facts and Evidence Worksheet to:*

- a. guide their inquiries and formulate views from the point at which a risk hypothesis has been developed through to the finalisation of position papers;*
- b. improve SME officers' (including those who sign off on compliance officers' work):*

- i. *ability to break down the elements of a legislative provision;*
  - ii. *to determine what constitutes facts and evidence;*
  - iii. *how to address conflicting pieces of evidence*
  - iv. *that affidavits are a form of evidence; and*
  - v. *what level of evidentiary burden is appropriate; and*
- c. *update worksheets as new information comes to light.*

ATO response: Agree

### **RECOMMENDATION 3.5**

*The ATO should improve IQF reviews of SME work, including:*

- a. *ensuring IQF review of S4 and HWI cases is done by experienced senior technical officers with expertise in S4 and HWI work (such as Case Leadership);*
- b. *stratifying IQF reviews according to the different population segments of the SME market;*
- c. *improving case assessors' access to HWI cases for independent review; and*
- d. *involving senior officers in open case reviews.*

ATO response: Agree

### **RECOMMENDATION 4.1**

*The ATO should develop indicators to measure how funding allocated directly to the COEs and tcn results in benefits to the sme business line.*

ATO response: Agree

## **RECOMMENDATION 4.2**

*For the purpose of obtaining end to end analyses of completed compliance cases, the ATO should extend the use of its 'case sequencing charts' to capture:*

- a. the reversal of liabilities in the cases' downstream dispute resolution steps;*
- b. the ATO's costs in the cases' downstream dispute resolution steps; and*
- c. estimated taxpayer costs for the total activities in cases (that is, cases' active compliance and downstream dispute resolution steps).*

**ATO response: Partially agree**

## **RECOMMENDATION 4.3**

*In order to appropriately minimise unnecessary compliance burdens on taxpayers and their advisers, the SME business line should:*

- a. continue to monitor the effectiveness of cycle times over the range of its compliance products and, in doing so, inform itself of the views of taxpayers and advisers who were involved in the compliance cases; and*
- b. enable SME officers to extend the cycle times in appropriate circumstances, without adverse impact on the taxpayer.*

**ATO response: Agree**

## **RECOMMENDATION 4.4**

*The SME business line should assess the effectiveness of its upstream risk identification processes in targeting likely non compliance and reducing compliance costs on compliant taxpayers. In conducting this assessment, the SME business line should inform itself from the analysis of the case sequencing charts and analysis of objections cases.*

**ATO response: Agree**

## **RECOMMENDATION 4.5**

*The ATO should improve management oversight and assurance measures to ensure SME officers proactively manage cases, including continually monitoring cases, re-communicating with*



*taxpayers and complying with the requirement to complete case plans before commencing compliance activities.*

ATO response: Agree

## **RECOMMENDATION 4.6**

*To reduce the risk of duplicating risk reviews for the same economic group, the ATO should improve its automated systems' ability to identify links between related entities within the same economic group.*

ATO response: Agree

## **RECOMMENDATION 4.7**

*To ensure that the ATO appropriately resources its compliance activities in relation to HWIs, S4 and Wealthy Australian taxpayers, the ATO should:*

- a. identify and fill gaps in resourcing (such as that identified in its internal report, 'Review of interpretative advice as part of the SM&E pipeline');*
- b. ensure that relevant information on workflows and resourcing is shared within the SME business line;*
- c. based on the increased complexity of this work, reassess the expected workloads of its SME Active Compliance, SME Interpretative Assistance (IA) officers and other ATO officers involved in dispute resolution (such as TCN and litigation);*
- d. assess the impacts of this compliance action on other SME business line commitments; and*
- e. sufficiently resource the SME's IA function to appropriately handle the number and complexity of objections being, and expected to be, lodged.*

ATO response: Agree

## **RECOMMENDATION 4.8**

*The ATO should improve staff understanding of the integration of the General Compliance, Wealthy Australians and HWIs areas and its impact on staff.*

ATO response: Agree

## RECOMMENDATION 5.1

*In consultation with taxpayers, tax practitioners and their representative bodies, the ATO should replace its 'Wealthy and wise' booklet (published in March 2008) with a new booklet to apply across the SME market segment that more clearly communicates what specific conduct taxpayers and their advisers can expect during compliance activities. This booklet should set clear expectations, including:*

- a. what the ATO will and will not do during compliance activities in the SME market segment (including HWIs and Wealthy Australians);*
- b. the manner in which those activities will be conducted; and*
- c. more effective escalation processes where the ATO's SME officers do not meet those expectations.*

**ATO response: Agree**

## RECOMMENDATION 5.2

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that at the outset of any compliance activity ATO officers will meet with the taxpayer and/or their representatives. The purpose of this meeting will include the following:*

- a. identify the areas to be reviewed or audited;*
- b. identify the information that the ATO is seeking and whether there are alternative forms of the information that would fulfil ATO purposes and be of reduced compliance burden to the taxpayer;*
- c. agree on the timeframes for the compliance activity and deadlines for key milestones in that activity; and*
- d. commit to the aim of 'no surprises' and the means to achieve that aim, such as periodic ongoing communication, preferred communication channels and escalation processes for any concerns arising during the audit.*

**ATO response: Agree**

## RECOMMENDATION 5.3

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that ATO officers will discuss and develop compliance activity case plans with the taxpayer's representatives before any activity commences. If there are*

*circumstances in which this opportunity was not to be afforded, these circumstances will be explicitly stated also.*

ATO response: Agree

## **RECOMMENDATION 5.4**

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that ATO officers, based on the relevant facts and evidence worksheet which they have prepared, will discuss potential views with taxpayers and their advisers before drafting a position paper that may have adverse impact on them.*

ATO response: Partially agree

## **RECOMMENDATION 5.5**

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that where the ATO's reasons for amending a taxpayer's liability change after assessments change (such as during the consideration of objections or litigation), the ATO will take fair and reasonable action to minimise the costs imposed on that taxpayer by reason of that change, including:*

- a. communicating the reasons why the new ATO position was not formulated earlier;*
- b. GIC remission; and*
- c. a concessional approach to penalty remission.*

ATO response: Agree

## **RECOMMENDATION 5.6**

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that the ATO will minimise taxpayers' costs arising from the change of SME officers during compliance activities. This will include, before engaging with the taxpayer or tax adviser the new compliance officer will:*

- a. familiarise themselves with the issues, facts and status of the compliance case; and*
- b. understand the information that has already been provided by the taxpayer and how that relates to the issues in question.*

ATO response: Agree

## **RECOMMENDATION 5.7**

*In relation to existing notification procedures concerning the commencement and finalisation of compliance activities, the SME business line should:*

- a. in addition to existing quality assurance measures, ensure that its officers comply with these procedures; and*
- b. more clearly set expectations about such notification by clearly and publicly stating when officers are to provide such notification.*

**ATO response: Agree**

## **RECOMMENDATION 6.1**

*The SME business line should require its compliance officers to use the facts and evidence worksheet to determine what information will be asked of a taxpayer in any particular compliance activity.*

**ATO response: Agree**

## **RECOMMENDATION 6.2**

*In the new booklet (which will replace the 'Wealthy and wise' booklet, as set out in recommendation 5.1), it should be stated that in relation to ATO information requests, the SME business line will:*

- a. clearly state to taxpayers and their advisers the time periods within which the ATO will review and respond to information provided by them; and*
- b. ensure that team leaders are progressing cases in a manner that provides taxpayers with adequate time to respond and minimises the time taken by SME officers to finalise cases.*

**ATO response: Agree**

## **RECOMMENDATION 6.3**

*The ATO should review, with their SME advisory group, the structure and content of any proposed new (or substantial alterations to existing) information gathering questionnaires.*

**ATO response: Agree**

## **RECOMMENDATION 6.4**

*The ATO should use the findings from the Risk Assessment Information Sharing project to develop improved information gathering and risk assessment and by communicating to each taxpayer the risks that the SME business line has identified in relation to that taxpayer.*

**ATO response: Agree**



## GLOSSARY

AC	the SME business line's Active Compliance area
CHPG	Closely held private group
COE	the ATO's Centres of Expertise area
CRR	Comprehensive Risk Review
FTE	Full-time equivalent
GC	the SME business line's General Compliance area
HOTSA	Health of the System Assessment
HWIs	High Wealth Individuals, with net wealth of over \$30 million
IA	the SME business line's Interpretative Assistance area
IQF	Integrated Quality Framework
ITI	Income Tax Investment, government funding
Larger SMEs	Small and Medium-sized enterprises with turnovers of between \$100 million and \$250 million
LBI	the ATO's Large business and internationals business line
MEI	the ATO's Micro-enterprise and individuals business line
NCAT	the SME business line's National Case Assessment Team
PRR	Preliminary Risk Review
S4 taxpayers	Entities with turnovers of between \$100 million and \$250 million
SNC	the ATO's Serious Non-Compliance area
TCN	the ATO's Tax Counsel Network area
TTTDM project	the ATO's tax technical decision making project
WAs	Wealthy Australians, those individuals with net wealth of between \$5 million and \$30 million

