



Australian Government

Inspector-General of Taxation

The Role of Inspector-General of Taxation in Australia

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1. INTRODUCTION

Revenue authorities are, by necessity, in the very unique position of being monopoly service providers to the community. Moreover, taxpayers do not benefit directly from the taxes that these authorities collect from them. The benefit is indirect and takes the form of provision of infrastructure and services such as health care and education.

There is also a perception of an information imbalance in that revenue authorities have or are able to collect a great deal about taxpayers who often feel there is a lack of transparency in the way the collected information is processed and used in compliance activities.

It is clear that there is a fundamental asymmetry in the relationship between revenue authorities and the taxpayer community that if left unchecked, can lead to public dissatisfaction, erosion of confidence in the tax system, decreasing levels of voluntary compliance and ultimately loss of revenue.

Given the unique position of revenue authorities, the above asymmetry can only be addressed through effective governance and scrutineering functions. Effective scrutineering functions have to be appropriately structured and resourced otherwise they cannot fulfil public expectations of holding to account large and well-resourced revenue authorities.

The ultimate 'owner' of the tax system is the community and parliament may be viewed as its board of directors. Parliament, often through its committees, seeks to hold the revenue authority accountable for the administration of the tax system. This is very valuable, however, it has limitations in terms of the capacity to deeply analyse and question the revenue authority.

Reviews of tax administration require the examination of significant amounts of information, including case files, correspondence and internal communications as well as meeting with relevant officers of the revenue authority. The parliamentary review processes are not designed for that level of scrutiny and are often reliant upon information provided by the revenue authority which may not always present the whole story or be perceived to suffer from a degree of inherent bias.

Taxpayers are also frequently reluctant or unwilling to raise their concerns with aspects of tax administration directly with the revenue authority or parliamentary committees. There appears to be a fear of retribution against taxpayers who publicly criticise the conduct or approaches of the revenue authorities.

Therefore, to effectively scrutinise the administration of the tax system by revenue authorities, the work of parliamentary committees needs to be augmented by other activities. These activities may be conducted by a taxpayer advocate group within the revenue authority (such as the National Taxpayer Advocate in the United States), as part of a broader scrutineering function of other government agencies (for example, ombudsman or national audit office type agencies), by a dedicated and specialised tax scrutineer agency (such as the Inspector-General of Taxation (IGT) in Australia), or by any combination of such agencies. This paper explores the evolution and current structure of the tax scrutineering function in Australia.

2. HISTORY

Pursuant to the *Inspector-General of Taxation Act 2003* (IGT Act), the IGT was established as an independent statutory officeholder to review systemic tax administration matters and make recommendations for improvement. These recommendations must be publicly reported and may be made to Government in relation to policy matters or to the Australian Taxation Office (ATO) on administrative issues.

Until recently, the investigation of single taxpayer complaints was the responsibility of the Commonwealth Ombudsman (Ombudsman) who handles complaints about federal government agencies more generally.

In the 2014 Federal Budget, the Government announced its decision to transfer the tax complaints handling function from the Ombudsman to the IGT.¹ The Budget announcement further expanded the IGT's scrutineering function to include the Tax Practitioners Board (TPB),² an independent statutory agency responsible for the registration and regulation of tax practitioners³ in accordance with the *Tax Agent Services Act 2009*.

The above Government decision took effect from 1 May 2015 and was aimed at enhancing "the systematic review role of the Inspector-General of Taxation and provide taxpayers with more specialised and focused complaint handling for tax matters."⁴ The Government decision was well received by stakeholders. The IGT had publicly advocated the creation of a single port-of-call for concerns with tax administration matters for some time to improve outcomes for taxpayers and the system more generally.

It should be noted that the Australian National Audit Office remains responsible for financial statement and performance audits of the ATO.

3. OVERVIEW OF THE EXPANDED ROLE AND FUNCTIONS OF THE IGT

Notwithstanding the significant expansion of the IGT's role over the past year, the overall aim of the IGT remains to "improve the administration of taxation laws for the benefit of all taxpayers, tax practitioners and other entities."⁵

The effectiveness of the IGT as a scrutineer stems from the actual and perceived independence of the office. The office of IGT is an independent Government agency which is wholly separate from both the ATO and the TPB. This is bolstered by its extensive and comprehensive review reports which are well-respected and have been influential in shaping the Australian tax administration landscape.

¹ Australian Government, *Budget Measures Budget Paper No 2 2014-15* (May 2014) p 217.

² Ibid.

³ Tax practitioners is a collective term to describe tax agents, business activity statement (BAS) agents and tax financial advisers.

⁴ Above n 1.

⁵ *Inspector-General of Taxation Act 2003*, s 3.

The structural separation of the IGT, its proven track record as well as its specialised focus and expertise has led to a high degree of trust and confidence from private sector stakeholders. There is, therefore, a greater willingness for them to candidly raise issues of concern and assist the IGT in improving tax administration.

The IGT recognises that the present structure of the Australian tax scrutineering function differs from that in some other countries, such as the United States (US), where the National Taxpayer Advocate is within the Internal Revenue Service and provides reports to Congress. The differences in this structure reflect the respective socio-political environment of the two countries. For example, members of the US Executive Branch are not part of the Legislature whereas in Australia, the Executive are members of the House of Representatives or the Senate in the Westminster tradition.

The role of the IGT has been likened to a 'safety valve' which provides transparency, accountability, confidence and integrity. In this respect, its role fosters trust and voluntary compliance by allowing issues to be ventilated and discussed by relevant decision makers so that concerns or issues may be appropriately addressed.

Effective scrutineering functions have to be appropriately resourced to hold to account large and well-resourced revenue authorities. It is instructive to note that concerns regarding the funding of relevant scrutineering functions as they relate to the ATO were previously considered by the Treasury in its *Australia's Future Tax System Review*.⁶

To ensure that both streams, i.e. single complaints and broader reviews, are effectively resourced, the IGT was allocated additional funding, as part of the 2014-15 Budget Measures, to recruit additional specialist staff and implement a new Information and Communication Technology platform.

Further discussion on the two main streams of the IGT's function is set out below.

3.1 COMPLAINT HANDLING

The transfer of the complaints handling function into the office of the IGT last year has enhanced the overall tax scrutineering capability and has facilitated a more co-ordinated approach, minimising duplication and overall costs. The benefits of the complaints handling and broader review functions being consolidated within the IGT may be summarised as follows:

- a single port-of-call for considering taxpayers' administration issues, simplifying and improving access;
- a more holistic understanding of taxpayer issues arising in relation to their dealings with the tax system;
- prompt systemic issues identification that emerges from handling a significant number of similar complaints;
- reduction of potential overlap between the current scrutineer agencies;

⁶ Treasury, *Australia's Future Tax System* (December 2009) p 663.

- stronger trust with internal and external stakeholders through effective and reciprocated consultation;
- better understanding of the subject matter and the tax environment;
- a specialist technical skills base, attracting specialist staff more effectively from a career perspective;
- minimised scrutineer resource allocation concerns as only the ATO is being scrutinised and not a broad range of government entities;
- economies of scale and scope in centralising the separate scrutineer functions; and
- greater synergistic benefits for the ATO in only having a single tax administration scrutineer agency.

As stated earlier, the IGT complaints handling function commenced on 1 May 2015. In the first 11 months of operations ending on 31 March 2016, we have received approximately 2,011 complaints of which 1,938 have been processed and finalised with the remainder in progress. Of the finalised cases, approximately 85 per cent are finalised within 15 business days.

Complaints may be received by the IGT through a number of channels. These include a smartform on our website, a dedicated telephone line, by mail, facsimile or through referrals from other government agencies including the ATO or the TPB themselves. On occasions, individuals may also make complaints to parliamentarians whom we have encouraged to direct such complainants to the IGT office.

The transfer of the complaints handling function afforded both the IGT and the ATO (and to a lesser extent the TPB) with an opportunity to redesign the complaints handling process. The redesigned process includes a number of features to improve the interaction between the ATO and the IGT, as well as providing a singular channel of access for taxpayers and their representatives to reduce cost and minimise duplication.

Firstly, the IGT aims to provide a high degree of assurance that complaints have been received and will be managed by the relevant officer. This is done through acknowledging complaints received within a 24 to 48 hour window and providing direct telephone contact details of the officer managing the case. Moreover, messages left on the IGT complaints voicemail are returned on the next business day with IGT officers assisting taxpayers to set out the details of their complaints and, again, providing direct contact details so that taxpayers are able to follow up on enquiries being managed by the IGT.

Secondly, all complaints received by the IGT are captured with any supporting documentation, synthesised and analysed for resolution. This minimises the resource impacts on the ATO whilst also reducing the need for the taxpayer to provide the same material multiple times particularly where the taxpayer re-approaches the IGT.

Thirdly, the taxpayer or tax practitioner is provided with an option to have the matter addressed directly by the ATO where the complainants have not availed themselves of the ATO's own complaints resolution processes. If this option is undertaken, the complaint is referred to the ATO Complaint section in the form of a Complaint Investigation Notice (CIN) from the IGT. Such complainants are informed that if they remain unsatisfied with the ATO's handling of their matter, they can re-approach the IGT.

Fourthly, the IGT formally tracks all complaints including those which are referred to the ATO. This provides independent assurance to taxpayers and tax practitioners that their matters have been registered and will be dealt with by an identifiable officer who is accountable for the management of their complaint.

Fifthly, pursuant to the amended IGT Act, the IGT is empowered to ask taxpayers to provide their Tax File Numbers (TFN) when lodging complaints, which was not previously available to the Ombudsman. The ability to request and provide TFNs enhances the ability of the ATO to quickly identify taxpayers on its systems to correctly pinpoint issues and identify options to resolve the matter.

Sixthly, as the IGT Complaints and Review team are tax specialists, we are able to engage meaningfully with taxpayers and ATO officers to identify the key issues for attention and highlight opportunities for resolution. The CIN, for example, sets out the key questions and issues needing to be addressed by the ATO. This approach has helped the IGT and the ATO to focus discussions, minimise the work needing to be undertaken by ATO officers and ensuring that issues critical to the resolution of the matter from the taxpayer's perspective are addressed.

Seventhly, the IGT and the ATO instituted 'Early Assessment Meetings' or 'EAMs' which are 15 minute discussions held within three to five business days after a CIN has been referred to the ATO. The purpose of the EAM is to narrow the areas of focus in the CIN, provide an opportunity for the ATO to surface additional facts or issues from its own review of the matter and to agree on actions to be taken, by whom and the relevant timeframes. The EAM seeks to ensure that only necessary inquiry and investigation aimed at resolving the matter is undertaken to minimise unnecessary actions, duplication of work and related costs for the ATO. Such a process has significantly reduced the average timeframes for complaints cases with approximately 85 per cent of matters being resolved or finalised within 15 business days.

Eighthly, through ongoing discussions between the IGT and the ATO, common areas of complaints are identified. Examples of such areas include delays in issuing Australian Business Numbers or delayed refund issues. These areas of complaint are generally capable of streamlined resolution processes. In such cases, the IGT and the ATO have developed pre-agreed processes against which these matters are handled effectively and efficiently and it is only in exceptional cases that the IGT has had to intervene further.

Ninthly, in more complex cases, the IGT engages directly with ATO senior management to provide 'early warning' of emerging risks and opportunities to address cases with sensitive issues through an escalation process that seeks to promptly explore options for resolution.

Finally, the IGT and the ATO continue to engage on a weekly basis in discussions and feedback on how each agency can improve their side of the process to deliver optimal outcomes to the community while minimising costs. The discussions have served as informal opportunities for continuous improvement, increased efficiencies and more effective outcomes for taxpayers and tax practitioners.

Although, the IGT cannot direct the Commissioner of Taxation (Commissioner) to take any particular action in respect of a taxpayer matter, the engagement of the IGT with complainants and the ATO has been beneficial in identifying key issues and options for resolution. It is early days but the effectiveness of such a strategy is evident in the high numbers of case closures, the short timeframes within which these are achieved and the substantial positive feedback already received.

We have been recruiting and training specialist staff to achieve an effective and efficient complaint handling service which enhances the taxpayers' experience. Further fine-tuning of our internal systems and processes as well as interactions with the ATO and TPB are being sought.

Once the complaints handling service is operating at optimal levels, we will be closer to realising our goal of gaining real-time insight into emerging issues and moving quickly to address problems before they escalate into major causes of taxpayer discontent. This could mean that in future, we may undertake more targeted reviews in an expedited manner to address particular areas where significant complaints have been received. We will also continue to consult with the community and conduct broader reviews as required.

3.2 BROADER REVIEWS

As set out above, since its inception, the IGT has been conducting broader reviews into systemic tax administration issues covering a broad range of topics that are relevant to all taxpayers from the very large businesses to micro businesses and individuals. The IGT has completed 42 reviews to date with another two in progress.

Generally, the IGT undertakes a review on his own motion based on stakeholder feedback and complaints received. Moreover, the Minister may request or direct the IGT to undertake a review on particular areas or issues. Requests may also be made by the Commissioner, the TPB, by resolution of either or both Houses of Parliament or by resolution of a Committee of either or both Houses of Parliament.⁷

In conducting these broader reviews, the IGT has been effectively engaging with the community by inviting submission and consulting with taxpayers, tax professionals and their representative bodies. Input from these stakeholders has been continually increasing as they become aware of the confidential nature of their dealing with the IGT as well as the fact that their issues are being heard and actioned through collaborative and robust engagement with the ATO.

The IGT review reports generally start by setting out the current status and stakeholder concerns. There are also comparisons made with the work and practices of revenue authorities in other jurisdictions as well as further independent research drawing on submissions made to the review. This naturally leads to recommendations for improvements which may be made to the ATO or the Government.

Neither the ATO nor the Government are compelled to accept IGT recommendations. However, the IGT review reports are made publicly available and include the ATO's response to each recommendation. It is noteworthy that the vast majority of the IGT's recommendations to the ATO have been accepted and implemented. Even where recommendations are not initially accepted, experience has shown that they may be subsequently taken on board and implemented. The Government has also implemented a number of the IGT's key recommendations.

The IGT maintains an active working relationship with the ATO and the Treasury on tax administration and related policy issues. Protocols are in place to guide interactions between the three agencies.

⁷ *Inspector-General of Taxation Act 2003*, s 8.

Furthermore, the IGT has strong powers of access to ATO information and personnel. The IGT may compel parties to provide any document and give evidence necessary for a review. This ensures that matters can be rigorously pursued and resolved.

The IGT may release his own reports. Only reports with policy recommendation for Government are required to be provided to the Minister for consideration. The Minister must ensure such IGT review reports are publicly released within 25 Parliamentary sitting days.⁸

Whilst a high degree of focus and resources have been directed to ensuring a seamless transition of complaints handling, the IGT has continued his work on broader reviews. Two announced reviews have been completed, a review at the request of the House of Representatives Standing Committee on Tax and Revenue was also completed and, as noted above, another two reviews are currently in progress.

4. PREVIOUS IGT REVIEWS

The IGT has undertaken reviews to examine a range of issues including the ATO's compliance approach to large businesses,⁹ small to medium enterprises (SMEs)¹⁰ and individual taxpayers¹¹. We have also examined key areas of tax administration including, improvements to the self-assessment system¹², the ATO's use of risk assessment tools¹³ and the ATO's use of alternative dispute resolution (ADR)¹⁴. The latter review provided a framework for the ATO's cultural shift towards greater taxpayer engagement to resolve disputes earlier and in a less costly manner.

Set out below are brief summaries of more recently completed IGT reviews. The full text of all published IGT reviews is available on the IGT website at www.igt.gov.au. The IGT also maintains a Twitter account (www.twitter.com/insp_gen_tax) through which the IGT announces new and upcoming work and reviews.

4.1 THE MANAGEMENT OF TAX DISPUTES

The *tax disputes review*¹⁵ arose from a request from the House of Representatives Standing Committee on Tax and Revenue (the Committee) to whom an Inquiry into Tax Disputes (the Inquiry) had been referred by the Acting Assistant Treasurer. The IGT was asked to focus on the large business and high wealth individual (HWI) themes of the Inquiry. One of the major issues to

⁸ *Inspector-General of Taxation Act 2003*, s 18.

⁹ IGT, *Report into the Australian Taxation Office's large business risk review and audit policies, procedures and practices* (2011).

¹⁰ IGT, *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* (2012).

¹¹ IGT, *Review into the Australian Taxation Office's compliance approach to individual taxpayers – use of data matching* (2014); IGT, *Review into the Australian Taxation Office's compliance approach to individual taxpayers – income tax refund integrity programme* (2014); IGT, *Review into the Australian Taxation Office's compliance approach to individual taxpayers – superannuation excess contributions tax* (2014).

¹² IGT, *Review into improving the self-assessment system* (2013).

¹³ IGT, *Review into aspects of the Australian Taxation Office's use of compliance risk assessment tools* (2014).

¹⁴ IGT, *Review into the Australian Taxation Office's use of early and alternative dispute resolution* (2012).

¹⁵ IGT, *The Management of Tax Disputes* (2015).

be considered by the Inquiry was whether a separate agency or a separate appeals area within the ATO should manage disputes or whether current arrangements should continue.

The *tax disputes review* drew on previous IGT reviews, submissions to the review and additional research and analysis including comparisons with the revenue authorities of the US, Canada, the United Kingdom, New Zealand and Ireland.

The review found that the underlying cause of many concerns raised in submissions appeared to be a lack of separation between the ATO's original decision makers and those officers who reviewed such decisions at the request of taxpayers. This had given rise to a lack, or perceived lack, of independence, leading taxpayers to believe that their cases were not reconsidered afresh and that they had been denied a fair hearing until reaching the Administrative Appeals Tribunal (AAT) or the Federal Court of Australia. Such views were supported by ATO statistics – for example during 2013–14, 85 per cent of taxpayer disputes were resolved without hearing once they reached the AAT.

Following earlier IGT reviews, the ATO had embarked on a programme of work to improve its compliance and dispute resolution approaches, particularly in relation to large businesses and HWIs. However, there was still a need for further improvements that could be sustainable and result in a more efficient, effective and transparent process being available to all taxpayers, particularly individuals and small businesses. Such improvements would also provide taxpayers with more confidence that they would be treated fairly and equitably.

The IGT's recommendation in this review was to create a separate and dedicated Appeals Group, led by a new Second Commissioner, to embed the improvements within the ATO structure and provide a framework that would be less dependent on the views and ideals of the ATO leadership of the day. The new Appeals Group would manage and resolve tax disputes for all taxpayers including the conduct of pre-assessment reviews, objections and litigation, as well as championing the use of ADR throughout the dispute cycle. The separation from both the ATO's compliance and legal advisory functions would also facilitate a fresh and impartial review of the taxpayer's case by empowering officers of the new area to resolve disputes through the most appropriate means, taking into consideration the individual circumstances of the taxpayer, their case and assessment of the ATO's precedential view. Additionally, the new area would ensure that settlements were appropriately scrutinised and in the best interests of the community.

In making the recommendation, the IGT sought to achieve the highest level of independence whilst retaining the dispute management function within the ATO. In this regard, the need for the Appeals Group to be headed by a new Second Commissioner was paramount, as such roles are statutorily appointed and their tenure and remuneration is pre-determined by the Government and the Remuneration Tribunal respectively and not the head of the relevant agency. Such an arrangement accords with comparable overseas jurisdictions and the views of the International Monetary Fund.

It is pleasing to see that the ATO has taken some steps towards implementing the recommendation by transferring all objection and dispute work from its compliance function to its legal advisory function. The creation of the Appeals Group as recommended in this review will require legislative change.

4.2 DEBT COLLECTION

The *Debt Collection*¹⁶ review was prompted by concerns raised by individuals, small businesses, tax and insolvency practitioners as well as their representative bodies. Broadly, these concerns related to the ATO's ability to recover tax debts effectively whilst ensuring that its actions were proportionate to circumstances of the affected taxpayers. The continual growth in collectable tax debt over the last decade to more than \$20 billion in 2013-14 and its potential impact on government services were also important considerations in undertaking this review.

During the review, the ATO acknowledged that its previous approach to debt collection could be improved as it involved a linear process for debt recovery which generally relied upon a series of escalated actions. Prior to the commencement of this review, the ATO had begun developing a programme of work to explore alternatives and improve its recovery action.

Given that the ATO's new programme of work would take some time to be fully implemented and bear fruit, the IGT made a number of recommendations as interim measures. One of these measures proposed a focus on the main debt holdings which are owed by individuals and micro businesses. These two taxpayer segments account for approximately 60 per cent (\$12.3 billion) of total collectable tax debt. Related recommendations were also made to identify underlying causes of cash flow and payment difficulties for these taxpayers and to develop preventative strategies. Another interim measure proposed that the ATO take more frequent and proportionate debt recovery action to minimise the necessity to take firmer action at a later time.

The ATO's new overarching strategic focus is to design actions that reduce overall debt holdings by using taxpayer behavioural analysis to prevent debts arising and, where they do arise, taking the most effective recovery action at the most appropriate time. This was consistent with recommendations made in previous IGT reviews where the use of behavioural analysis was a common theme. The IGT continues to endorse such an approach.

The IGT also identified a need to ensure ATO officers have the appropriate level of expertise and experience to handle taxpayer cases and fulfil procedural requirements. The ATO has a framework for officer decision authorisations and also provides training and support for various aspects of debt recovery. The decisions of officers, who are considered 'proficient', are not scrutinised in the majority of low risk debt cases. Given the sustained and substantial level of individual taxpayer complaints, the IGT considered that there is a need for greater top-down supervision and recommendations were made accordingly.

Overall, the IGT made 19 recommendations with 16 of which the ATO has agreed, agreed in principle or agreed in part. The ATO has disagreed with 2 recommendations and considered that 1 recommendation was a matter for Government. One of the disagreed recommendations required the ATO to merge its Debt Business Line into the Compliance Group although the ATO has indicated it would consider such a merger as part of its broader cultural and structural change.

4.3 ATO SERVICES AND SUPPORT FOR TAX PRACTITIONERS

There is a high degree of taxpayer reliance on the services provided by tax practitioners in Australia. They assist approximately 70 per cent of individual and 90 per cent of business taxpayers to comply with their tax obligations. Tax practitioners are also an invaluable source of knowledge and practical experience which may be drawn upon to develop more effective and

¹⁶ IGT, *Debt Collection* (2015).

efficient tax laws and administrative practice. Accordingly, maintaining a positive relationship between the ATO and tax practitioners is critical to the functioning of the self-assessment system.

The review into the ATO's services and support for tax practitioners was undertaken in response to concerns raised by the latter and their representative bodies in relation to access and adequacy of ATO support and services and the resulting strained relationship between tax practitioners and the ATO.

A key underlying cause of the strain on the ATO-tax practitioner relationship has been the reliability and functionality of the ATO Portals – gateways through which tax practitioners can use a range of ATO services. The ATO Portals have been described as an indispensable tool of trade and 'the most useful tools that the ATO has ever provided'. However, in recent years, their unreliability has been a major source of tax practitioner concern and frustration as they believe it has resulted in productivity loss, missed deadlines, irrecoverable costs as well as damage to their reputation and relationship with their clients.

The ATO has acknowledged the concerns with the ATO Portals and believes that it will address the majority of tax practitioner concerns in the long term by migrating to a 'more functional software platform and flexible online system.' However, such a migration causes further uneasiness for tax practitioners because of their previous experience with the ATO's deployment of new technology. In this regard, the IGT took comfort from the ATO's approach to maintaining the current ATO Portals and operating them in parallel with the new system.

At the closing stages of this review, the ATO advised that it estimated the migration to occur within the next two years. During this time, the ATO would not seek to implement key improvements sought by tax practitioners to the current ATO Portals but will limit enhancements to maintenance and stability assurance. Therefore, it is likely that some of the tax practitioner concerns and frustration may persist in the short term.

Another source of concern for tax practitioners has been the accuracy of ATO information and ATO communications which they believe has, in some instances, generated unnecessary follow up work and costs for them. The IGT recommended improved communication by user-testing standardised correspondence to ensure that the tone and content are effective in generating the intended behavioural response and minimise unnecessary contact.

Tax practitioners had also raised concerns with the delays and quality of support provided on the ATO's website and telephone services. In this regard, the IGT recommended improved ATO telephone services by maintaining shorter wait times, having technically proficient staff to answer calls, simplifying the proof of identity processes and improving the ATO's website by taking into account tax practitioners' needs.

Overall the IGT made eight recommendations, with which the ATO has agreed fully or partially.

4.4 ATO MANAGEMENT OF TRANSFER PRICING MATTERS

This review was prompted by concerns, from taxpayers, tax professionals and their representative bodies, with the unnecessary costs and protracted timeframes involved in the ATO's transfer pricing compliance activities, lack of ATO communication on important issues, inadequate public advice and guidance and ineffective use of consultative forums. The key underlying theme was insufficient ATO capability to deal with transfer pricing matters.

Internationally, there were also government and community concerns regarding risks to revenue arising from transfer pricing, base erosion and profit shifting as evidenced in the OECD and G20 forums. This was also an important consideration in undertaking this review.

The review found that key causes of the concerns were inadequate succession planning and resource management. Experienced specialist officers had left the ATO's transfer pricing area and their knowledge was not effectively disseminated across the organisation. Another significant cause was the complex interactions between the ATO's internal functions and a lack of clarity with respect to the decision-making process.

A suite of recommendations were made to develop sufficient organisational capability to address transfer pricing risks, including giving priority to measures that target the highest risks to tax revenue. A number of recommendations were also made to optimise the use of current ATO resources while further capability was being developed. In this regard, the ATO agreed to match the scope and scale of transfer pricing compliance activities with the available specialist capability. In addition, the ATO also agreed to limit the use of wide-ranging enquiries to identify emerging risks and give priority to project-based compliance activities that target the highest revenue risks.

In addition to responding to ATO enquiries, taxpayers' transfer pricing tax obligations, such as documenting the evidence for arm's length pricing outcomes, impose substantial costs. These costs have a regressive effect, particularly for SMEs. As a result, the ATO agreed to a number of recommendations aimed at reducing the compliance burden for SME taxpayers including the increased use of safe harbours for lower value and more common transactions.

The review also focused on the administration of the Advanced Pricing Arrangement (APA) programme which provides opportunities to reduce overall compliance costs by reaching a common understanding of views through a cooperative process. The IGT observed that the use of APAs for more complex arrangements was critical to maintaining taxpayer and broader perceptions of the utility of the programme and therefore identified a need for greater ATO transparency on the reasons for 'audit-like' approaches in APA processes and the circumstances which would justify a transition to an audit. It was also noted that such APAs are expected to provide valuable intelligence on emerging business practices and issues. In this respect, the ATO agreed to promote the use of the APA programme, provide the criteria for the withdrawal from APA negotiations and improve communications with taxpayers on issues of concern. However, the ATO has not agreed to certain suggested improvements with respect to APAs including better resourcing and a 'stage and gate' process.

Overall, there are 18 recommendations, 17 of which the ATO has agreed with in whole, part or principle.

4.5 ATO ADMINISTRATION OF PENALTIES

Concerns with the ATO's administration of penalties had been persistently raised with my office over a number of years. In some previous reviews, particularly the self-assessment review, the IGT made recommendations in this regard. However, due to the level of concern and its ongoing nature, the penalties review was undertaken to more broadly examine the issues being raised.

The report found that approximately 25 per cent of total penalties raised were later reduced due to unsustainable penalty decisions. Accordingly, the IGT made recommendations for the ATO to improve its penalty decision-making capability (through such means as further development of officers), the clarity and practicality of guidance material as well as its processes for identifying, collecting and analysing penalty information. In relation to taxpayer perceptions that penalties

may be used as leverage to influence primary tax disputes, the IGT made a number of other recommendations including only requiring taxpayers to pay penalties after primary tax disputes have been settled and that discussions on potential penalties be delayed until after position papers have been issued.

The IGT also encouraged the Government to consider reviewing the penalty regime to promote greater voluntary compliance, and in particular to address issues such as a lack of sufficient differentiation between a range of taxpayer behaviours and the inability of taxpayers to be compensated for time-value of money paid for unsustained penalties. As a result, the Government announced its intention to consider these issues once the Tax White Paper process has been finalised.

5. UPCOMING IGT REVIEWS

As mentioned earlier, the IGT has two reviews in progress, namely the *review into the ATO's employer obligations compliance activities* and the *review into the Taxpayers' Charter and taxpayer protections*. The latter review examines the adequacy of existing taxpayer rights including compensation to taxpayers where they have suffered loss or damage caused by ATO actions. The full text of the terms of reference for this review is reproduced in the Appendix.