



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

# GST Refunds

Inspector-General of Taxation

March 2018





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16 March 2018

The Hon Kelly O'Dwyer MP  
Minister for Revenue and Financial Services  
Parliament House  
Canberra ACT 2600

Dear Minister

**Inspector-General of Taxation (IGT) Review into Goods and Services Tax Refunds**

I am pleased to present you with my report of the above review which has examined the Australian Taxation Office's (ATO) approach to verifying GST refund claims before issuing them.

This review arose out of concerns raised by both individuals and businesses through the IGT complaints handling service as well as by stakeholders in the development of my current work program. These concerns largely centred on undue delay and insufficient engagement between the ATO and taxpayers during the verification process.

Overall, the ATO's approach to GST refund verification is operating well with the vast majority of refunds being released without the need for verification and, of those that are stopped, over 50 per cent are processed and released within 14 days.

I have identified some opportunities for improvement in relation to the strike rates achieved by the ATO's automated risk assessment tools, communication between the ATO and taxpayers and their representatives as well as promoting greater awareness of options when taxpayers are experiencing financial hardship. I have made 5 recommendations (comprising 16 parts) to the ATO with all of which it has either agreed in full or in part (11 out of 16 parts).

The review also examined the ATO's current approach to using refund retention as part of a broader project to address fraud within the precious metals industry and the difficulties associated with that approach. I have made one recommendation for the Government's consideration regarding possible amendments to the legislation to better empower the ATO to address serious risks of fraud.

I offer my thanks to the government agencies, professional bodies, tax practitioners and taxpayers who have contributed and provided their support to this review.

Yours faithfully

Ali Noroozi  
Inspector-General of Taxation



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## EXECUTIVE SUMMARY

The Inspector-General of Taxation's (IGT) review into Goods and Services Tax (GST) refunds arose from concerns raised through the IGT's complaints handling service and during consultation to develop the 2017 work program. These concerns included the accuracy of the ATO's risk assessment tools, its engagement with taxpayers and its efforts to minimise adverse impacts on affected taxpayers.

The IGT has reviewed the end-to-end process involved in refund verification including from initial case selection through to the review and audit activities. Overall, the IGT has found that the ATO's administration of GST refunds operated efficiently with the vast majority of refunds released without being stopped for verification. Moreover, where refunds are stopped, the majority were processed and released within 14 or 28 days.

Some opportunities for improvement have been identified including processes to enhance the ATO's automated risk assessment tools which have been achieving a strike rate of only 26.7 per cent (approximately 1 in 4 cases) and which the ATO has acknowledged to be no better than random selection. Furthermore, the IGT has identified that the ATO can streamline its instructions and guidance to staff when interacting with taxpayers, taking into account their circumstances and the adverse financial impacts that delayed refunds can have on their cash flow.

The IGT made 5 recommendations (comprising 16 parts) to the ATO which were aimed at:

- developing a framework for continuous improvement of its automated risk assessment tools;
- streamlining its guidance to staff and implementing tools to assist them in complying with their obligations under section 8AAZLGA of the *Taxation Administration Act 1953*;
- enhancing its information requests to taxpayers and providing a channel for pre-emptive provision of such information;
- improving its notification of when taxpayers' objection rights to the retention of refunds has been triggered and assisting them to lodge such objections effectively; and
- raising awareness of staff and taxpayers about financial hardship issues, appropriately considering them and enabling automated partial release of refunds.

The ATO has agreed in full or in part with all 5 recommendations (11 out of 16 parts).

During the course of the review, it became apparent that particular concerns were emerging in relation to the ATO's use of refund retention to address risks of serious fraud within the precious metals industry. The IGT has acknowledged the seriousness of these fraud risks but has also noted the prolonged timeframes to finalise such cases. Accordingly, the IGT has also recommended to the Government to consider amending the relevant provision to allow the ATO to effectively investigate and address risks of fraud the seriousness of which has been established.



# LIST OF RECOMMENDATIONS

## RECOMMENDATION 3.1

*The IGT recommends that the ATO:*

- (a) *develop a formal framework of continuous improvement for its risk assessment tools which includes:*
  - (i) *periodic reviews with clear milestones;*
  - (ii) *ensuring that case officers are consistent and accurate in reporting case related data and other pertinent matters in all relevant cases;*
  - (iii) *improving intelligence capture through greater engagement between risk managers and operational teams across different business lines such as Indirect Tax and Smarter Data;*
  - (iv) *developing a suite of performance reports for use within the Indirect Tax business line and ATO Executive Committees; and*
- (b) *prioritise the deployment of the On-Line BAS Check tool.*

## RECOMMENDATION 4.1

*The IGT recommends that, in respect of pre-issue GST refund verification, the ATO:*

- (a) *consolidate and streamline its guidance to its officers with an emphasis on adhering to the statutory requirements;*
- (b) *ensure that interactions between its officers and taxpayers as well as its officers' consideration of statutory requirements are accurately and consistently documented and that team leaders use such documentation to assess the performance of officers and the taxpayer experience;*
- (c) *provide a mechanism to automatically alert its officers and team leaders to notify taxpayers of the retention of their refunds within the statutory period; and*
- (d) *improve its communication with taxpayers by ensuring that they are provided with sufficient reasons for the retention of their refunds and the other information provided to them is accurate and up to date.*

## RECOMMENDATION 4.2

*The IGT recommends that, in undertaking pre-issue GST refund verification, the ATO:*

- (a) *periodically review its information requests templates with input from stakeholders, including industry experts, to ensure that those requests are appropriately focused on addressing the risks identified; and*
- (b) *consider allowing taxpayers and tax practitioners to pre-emptively provide information online to assist in the timeliness of the verification process.*

### **RECOMMENDATION 4.3**

*The IGT recommends that the ATO:*

- (a) make effective use of its automated system to calculate the 60-day period within which taxpayers may lodge an objection and inform them accordingly; and*
- (b) provide information to assist taxpayers in lodging such objections effectively.*

### **RECOMMENDATION 5.1**

*The IGT recommends that the ATO:*

- (a) improve access to and raise awareness of taxpayers, tax practitioners and its own officers about assistance available in serious financial hardship cases including full or partial release of GST refunds;*
- (b) ensure that the appropriate consideration of the financial impact on taxpayers, as required by paragraph 8AAZLGA(2)(c) of the TAA 1953, and serious financial hardship claims are carefully documented; and*
- (c) develop an automated system for the partial release of GST refunds.*

### **RECOMMENDATION 6.1**

*The IGT recommends that the Government consider amending section 8AAZLGA of the TAA 1953 to allow the Commissioner, in appropriate cases, to effectively investigate and address risks of fraud the seriousness of which has been established by means such as obtaining a Federal Court order.*

# CHAPTER 1 - CONDUCT OF THE REVIEW

1.1 The Inspector-General of Taxation (IGT) has conducted this review into the Australian Taxation Office's (ATO) verification of Goods and Services Tax (GST) refunds in response to stakeholders' concerns<sup>1</sup> which were raised through the complaints handling service and again during consultation on the 2017 work program.

1.2 Terms of reference for the review were announced on 5 April 2017, a copy of which appears in Appendix 1. The report itself is produced pursuant to paragraph 7(1)(f) of the *Inspector-General of Taxation Act 2003* (IGT Act 2003).

1.3 The IGT received a range of submissions and also engaged with a number of stakeholders including taxpayers, tax practitioners and their representative bodies as well as senior staff in other government departments to gain a better understanding of the issues and areas requiring improvement. The concerns raised may be broken down into the three broad themes:

- the accuracy of the ATO's risk assessment tools to detect incorrect or potentially fraudulent GST refunds;
- the adequacy of the ATO's engagement with taxpayers and their representatives during the GST refund verification process; and
- the adverse impacts that delayed GST refunds may have on taxpayers.

1.4 In addition, the IGT has been approached by a number of businesses operating within the precious metals industry (as well as their representatives) through the complaint handling service. In the main, their concerns relate to the intensity of the ATO's actions within the industry, the significant delays in issuing refunds and the corresponding financial and personal impacts on affected taxpayers.

1.5 It should be noted at the outset that this report is not intended to be broad examination of the ATO's administration of the GST, rather, it examines discrete aspects of the GST refund verification process. Other risks within the GST system, such as Input Tax Credit (ITC) inflation and more serious fraud activity may be considered in other IGT reviews, such as the *Review into the ATO's Fraud Control Management* (AFCM).<sup>2</sup>

1.6 The IGT review team has worked progressively with the ATO to distil potential areas for examination and to agree on specific improvements. This work has involved discussions with ATO officers in the Indirect Tax (ITX) business line, being the overall area responsible for GST refunds, as well as ATO senior management. As part of the IGT's independent assurance process, case records on the ATO's case management system, Siebel, and performance statistics have been examined and analysed to better understand taxpayer concerns.

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<sup>1</sup> This review was commenced pursuant to paragraph 7(1)(d) of the *Inspector-General of Taxation Act 2003*.

<sup>2</sup> Inspector-General of Taxation (IGT), *Review into the Australian Taxation Office's Fraud Control Management* (2017 – in progress) <[www.igt.gov.au](http://www.igt.gov.au)>.

1.7 The Commissioner of Taxation (Commissioner) was provided with an opportunity to make submissions on any implied or actual criticisms in this report.<sup>3</sup>

## STRUCTURE OF THE REPORT

1.8 As mentioned earlier, this report examines discrete aspects of the GST refund verification process and is divided into the following chapters:

- (a) Chapter 2 provides a brief history and overview of the GST system with a focus on GST refunds;
- (b) Chapter 3 evaluates the effectiveness of the ATO's case selection process for retaining refunds for verification purposes;
- (c) Chapter 4 explores the ATO's processing of cases identified for pre-issue verification and considers how the ATO engages with taxpayers throughout this process;
- (d) Chapter 5 examines the impact that the ATO's verification activities may have on affected taxpayers and the options available to mitigate these impacts; and
- (e) Chapter 6 considers the specific experience of the precious metals industry, in an administrative context, which has more recently been subjected to GST refund verification.

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<sup>3</sup> In accordance with sub-section 8(5) of the *Ombudsman Act 1976* which has effect by virtue of section 15 of the *Inspector-General of Taxation Act 2003*.

## CHAPTER 2 - BACKGROUND

### THE GST SYSTEM

2.1. The GST was introduced on 1 July 2000 to replace the Sales Tax and certain State taxes.<sup>4</sup> The Sales Tax had commenced in 1930 and was imposed on the last wholesale sale of goods for consumption in Australia.<sup>5</sup> The manner in which this was achieved was by way of an exemption system, such that the tax was only applied at the final point of consumer sale. As a result, there was no need for a credit and refund process as is the case in GST or Value Added Tax (VAT). When Sales Tax was introduced, goods accounted for the bulk of Australia's economic activity, which is reflective of the more limited nature of services available for consumption at that time.<sup>6</sup>

2.2. In the early 1970s, the McMahon Government announced a review into the existing Australian tax system. On 31 January 1975, the report of the review, known as the Asprey Report, was released.<sup>7</sup> One of the recommendations contained in the Asprey Report was to introduce a broad-based GST or VAT which had been adopted by countries in Europe and South America. Despite discussions that followed, this recommendation was not implemented at the time.

2.3. Decades later, the Howard Government, as part of its election campaign, proposed the introduction of a GST to replace the Sales Tax. It argued that by the late 1990s, the production of goods constituted less than one-third of the national economy. As a result, the Sales Tax base was declining and it impacted the revenue to fund government services.<sup>8</sup> Additionally, the Sales Tax system penalised Australian producers who were exporters or who otherwise competed with importers.<sup>9</sup>

2.4. The GST was enacted as part of the *A New Tax System*<sup>10</sup> suite of reforms. The tax is levied at 10 per cent on most goods and services consumed in Australia. Under the GST system, the tax is economically borne by the final consumer but is collected and paid by other entities in the supply chain. 'Entity' is a term used in the relevant legislation in an important collective sense. It encompasses a broad range of businesses, not-for-profit organisations, government agencies and legal persons including bodies corporate, but for ease of reference and reader familiarity, this report makes reference to 'taxpayers' throughout instead of 'entity' unless context requires otherwise.

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4 Explanatory Memorandum, House of Representatives, *A New Tax System (Goods and Services Tax) Bill 1998*.

5 Peter Costello M.P., *Tax Reform: Not a New Tax, A New Tax System*, (Treasurer of the Commonwealth of Australia, 1998).

6 Ibid.

7 Taxation Review Committee, Parliament of Australia, *Full Report*, (1975) p 523.

8 Costello, above n 5.

9 Ibid.

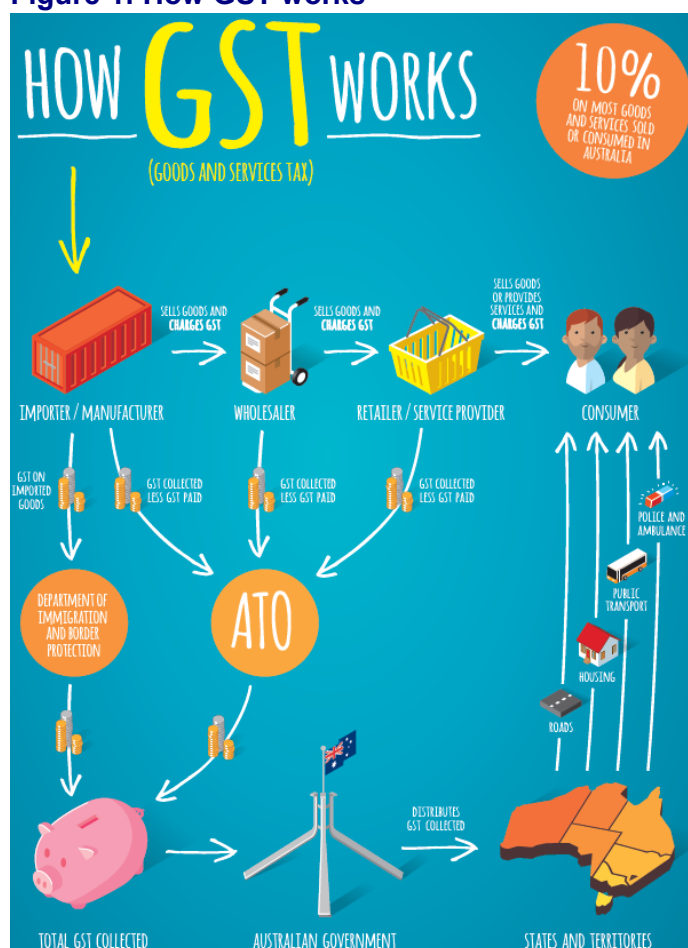
10 *A New Tax System (Goods and Services Tax) Act 1999*.

2.5. Goods and services are classified as taxable, GST-free or input taxed.<sup>11</sup> Where goods and services are GST-free or input taxed, GST is not charged on the supply of those goods or services<sup>12</sup> although in the latter case no refund or ITCs are allowed.

2.6. The manner in which GST is collected and remitted to the ATO is via a registration system using the Australian Business Number (ABN). Registered taxpayers include GST in the price charged for the goods and services and remit these amounts to the ATO. Registered taxpayers are entitled to claim ITCs for the GST paid for goods and services. For example, this may include taxpayers such as retailers who purchase goods which will subsequently be on-sold to the final consumer. Therefore the final 'consumer' effectively pays for the GST included in the final sale price as they are not able to register to claim ITCs.

2.7. The ATO's illustration of how GST works is shown in Figure 1 below.

**Figure 1: How GST works**



Source: ATO

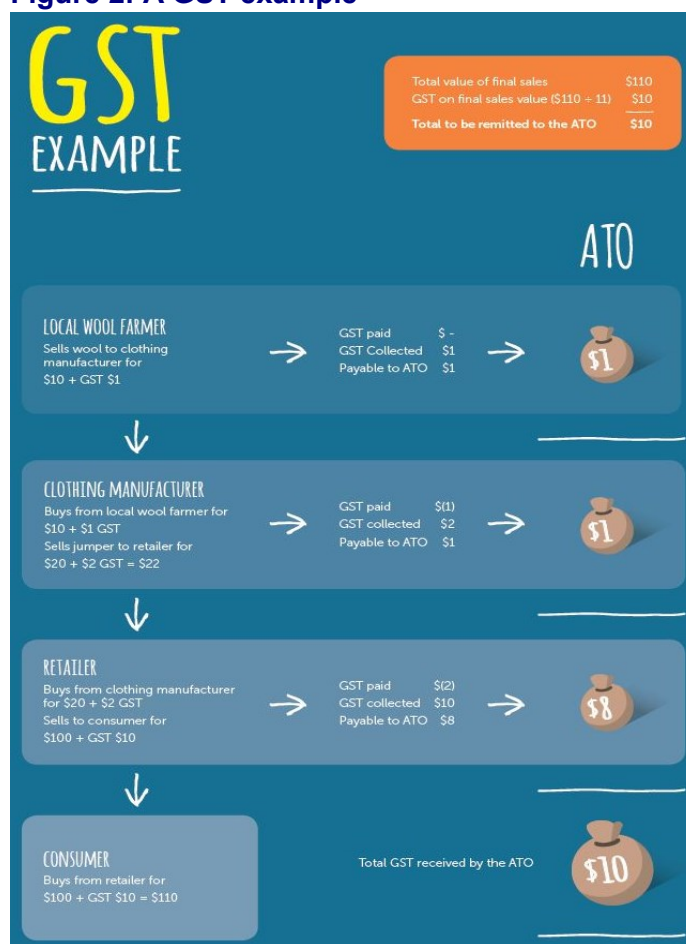
11 In VAT systems, the corresponding expressions used are Standard Rated for taxable supplies, Zero-Rated for GST Free and Exempt for Input-Taxed supplies.

12 A New Tax System (Goods and Services Tax) Act 1999 s 9-30.



2.8. As set out in the diagram above, the GST system operates at each step of the manufacturing, wholesale and retail process, with each participant ultimately collecting a portion of the total GST during their specific transaction and remitting it to the ATO. Total GST collected is made available to the Federal Government to apportion amongst the States and Territories in line with specific agreements (net of any ITCs which are not illustrated in the diagram). A simplified numerical illustration of the GST flows through the different manufacturing and sale stages to the final consumer and net GST payments to the ATO is depicted in Figure 2.

**Figure 2: A GST example**



Source: ATO

2.9. The Australian GST system is similar to other comparable jurisdictions, namely, the United Kingdom (UK), Canada and New Zealand. In these jurisdictions, GST or VAT is also charged on most goods and services with entities, such as businesses, collecting and paying the tax to the relevant revenue authority. In comparison to these jurisdictions, Australia has one of the lowest GST rates. The UK's VAT rate is 20 per cent.<sup>13</sup> In Canada, the GST rate varies from 5 per cent to 15 per cent between different provinces<sup>14</sup> and in New Zealand, the GST rate is 15 per cent.<sup>15</sup>

<sup>13</sup> Gov.uk, *VAT rates* (16 June 2017) <[www.gov.uk](http://www.gov.uk)>.

<sup>14</sup> Canada Revenue Agency, *Charge the GST/HST* (13 December 2016) <[www.cra-arc.gc.ca](http://www.cra-arc.gc.ca)>.

<sup>15</sup> New Zealand Inland Revenue, *About GST* (16 February 2016) <[www.ird.govt.nz](http://www.ird.govt.nz)>.

2.10. Once GST is collected, the Commonwealth Grants Commission recommends how the GST should be distributed to each State and Territory to achieve 'horizontal fiscal equalisation' as per the intergovernmental agreement reached between the Commonwealth, States and Territories.<sup>16</sup>

## THE ROLE OF REFUNDS IN THE GST SYSTEM

2.11. Registered taxpayers are generally responsible for collecting and remitting GST and the ATO is responsible for the administration of the GST, as illustrated in Figures 1 and 2 above. If the GST collected within a reporting period exceeds the ITCs, taxpayers are required to pay the net GST amount to the ATO. These amounts are reported on a taxpayer's Business Activity Statement (BAS)<sup>17</sup> and forwarded to the ATO. Depending on the taxpayer's circumstances, such reporting takes place monthly, quarterly or annually.<sup>18</sup>

2.12. Where a taxpayer's ITCs exceed the total GST charged within a reporting period, they are entitled to a refund. The amount of GST refunds issued each year is significant. For example, in the 2015-16 financial year, the ATO issued BAS refunds totalling \$54.2 billion (of which, a very large proportion is GST).<sup>19</sup> By way of completeness, it should be noted that the reason total BAS refunds may be higher than GST refunds is that the BAS also includes other kinds of tax refunds such as those associated with Luxury Car Tax and Wine Equalisation Tax.

2.13. The ATO has committed to finalising 94 per cent of BASs lodged electronically within 12 business days and 80 per cent of paper lodgments within 50 business days.<sup>20</sup> In the 2016-17 financial year, the ATO reported that it had met these performance targets in 100 per cent of cases.<sup>21</sup>

2.14. Due to the periodic nature of the reporting of GST, a timing difference may arise between the GST paid for purchases and the lodgment of the BAS and the related refund issuing. For example, generally for an entity that reports on a quarterly basis, purchases made in early April would not be reported until July. Similarly, those reporting on a monthly cycle would not be able to report and claim any refunds until the following month.

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16 Commonwealth Grants Commission, *About the CGC* <[www.cgc.gov.au](http://www.cgc.gov.au)>; Council of Australian Governments, *Intergovernmental Agreement on Federal Financial Relations* (2008) <[www.cgc.gov.au](http://www.cgc.gov.au)>.

17 Certain legislative and explanatory documents, as well as court decisions, refer to 'GST returns'. The GST return forms a part of an entity's Business Activity Statement (BAS) and it is the BAS that is retained for verification. For consistency, this report will use the term BAS rather than GST return.

18 Australian Taxation Office (ATO), *Options for reporting and paying GST* (16 June 2015) <[www.ato.gov.au](http://www.ato.gov.au)>.

19 Commissioner of Taxation, *Annual Report 2015-16* (2016) p 40.

20 ATO, *Current year commitments to service* (24 July 2017) <[www.ato.gov.au](http://www.ato.gov.au)>.

21 Commissioner of Taxation, above n 19, p 225.

2.15. As a result of the timing difference and the accounting or attribution method used, a taxpayer's cash flows may be affected positively or negatively.<sup>22</sup> The prompt processing and issuing of net GST refunds is critical in alleviating cash flow pressures, particularly for small businesses or those businesses operating in industries with low margins. However, the ATO is also tasked with responsibility of upholding the integrity of the GST system which it may carry out by verification processes prior to paying GST refunds (sometimes called pre-issue verification). Once verification checks are satisfactorily reviewed by ATO officers, GST refunds are paid to taxpayers.

2.16. Similar to Australia, taxpayers in the UK, Canada and New Zealand lodge returns with their revenue agency to claim refunds. In the UK, HM Revenue and Customs (HMRC) usually pays VAT refunds within 10 working days of receiving the return.<sup>23</sup> In New Zealand, the Inland Revenue Department is required to issue GST refunds no later than 15 working days after the return is received.<sup>24</sup> Similarly in Canada, GST refunds are issued generally within two weeks if the return is lodged electronically.<sup>25</sup>

## THE ATO'S HISTORICAL APPROACH TO GST REFUND VERIFICATION

2.17. Prior to 2011, the ATO had relied on its general powers of tax administration, and the implied time afforded to it under section 35-5 of *A New Tax System (Goods and Services Tax) Act 1999* (GST Act) to retain GST refunds for verification purposes prior to payment of the refund. Effectively, the ATO was of the view that it had the right to retain the refunds until it had established the accuracy of the claim.<sup>26</sup> It also believed that such an approach was consistent with the *Financial Management and Accountability Act 1997* and the *Taxation (Interest on Overpayments and Early Payments) Act 1983*, which requires the ATO to pay interest to the taxpayer for processing payments and credits after the periods specified.<sup>27</sup>

2.18. Up until 2011, the legal basis for the above approach was not challenged through the courts or examined by any scrutineers of ATO activities.<sup>28</sup>

## THE MULTIFLEX DECISION

2.19. The ATO's ability to retain GST refunds for verification was considered by the Federal Court of Australia in the case of *Multiflex Pty Ltd v Commissioner of Taxation*<sup>29</sup> (*Multiflex*) and subsequently upheld on appeal by the Full Federal Court.<sup>30</sup>

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22 *A New Tax System (Goods and Services Tax) Act 1999*, pt 2-6 div 29.

23 Gov.uk, VAT repayments (15 June 2017) <[www.gov.uk](http://www.gov.uk)>.

24 *Goods and Services Tax Act 1985* (NZ).

25 Canada Revenue Agency, *After filing a GST/HST return*, (20 October 2016) <[www.cra-arc.gc.ca](http://www.cra-arc.gc.ca)>

26 *Multiflex Pty Ltd v Commissioner of Taxation* (2011) 81 ATR 347, 349 at para 3.

27 Explanatory Memorandum, House of Representative, Tax and Superannuation Laws Amendment (2012 Measures No. 1) Bill 2012, p 71.

28 House Standing Committee on Economics, Parliament of Australia, *Advisory Report on the Tax Superannuation Laws Amendment (2012 Measures No.1) Bill 2012* (2012) pp 14-15.

29 *Multiflex Pty Ltd v Commissioner of Taxation* (2011) 81 ATR 347.

30 *Commissioner of Taxation v Multiflex Pty Ltd* (2011) 197 FCR 580.

The Commissioner had retained Multiflex's GST refunds while conducting an audit into the legitimacy of the claims that were suspected to be part of a fraudulent scheme.

2.20. The Federal Court at first instance decided that the 'reasonable time' referred to in section 35-5 of the GST Act is the period that the Commissioner takes to facilitate the payment of the GST refunds and does not include the time taken to conduct an investigation into the accuracy of the claims. The Commissioner was ordered to pay the GST refunds to Multiflex before the audit was finalised.<sup>31</sup>

2.21. The Commissioner appealed to the Full Federal Court, which handed down its decision on 11 November 2011.<sup>32</sup> The Full Federal Court upheld the first instance decision. The Commissioner's application for special leave to appeal to the High Court was refused on 9 December 2011.<sup>33</sup>

2.22. The Full Federal Court in dismissing the Commissioner's appeal determined that the Commissioner did not have any additional time to investigate the accuracy of BASs. The Court noted:

*If that be a defect in the scheme of taxation, the defect is one for Parliament to address.*<sup>34</sup>

2.23. The ATO issued a decision impact statement on 12 December 2011 accepting that the Commissioner could raise an assessment if he considered the reported amounts were incorrect.<sup>35</sup>

## SECTION 8AAZLGA AND THE ATO'S CURRENT GST REFUNDS APPROACH

2.24. Following the *Multiflex* decision, Parliament took action to ensure that the Commissioner had the ability to delay refunding amounts in certain circumstances<sup>36</sup> by enacting section 8AAZLGA of the *Taxation Administration Act 1953* (TAA 1953):

- (1) *The Commissioner may retain an amount that he or she otherwise would have to refund to an entity under section 8AAZLF, if the entity has given the Commissioner a notification that affects or may affect the amount that the Commissioner refunds to the entity, and:*
  - (a) *it would be reasonable to require verification of information (the **notified information**) that:*
    - (i) *is contained in the notification; and*
    - (ii) *relates to the amount that the Commissioner would have to refund; or*

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31 *Multiflex Pty Ltd v Commissioner of Taxation* (2011) 81 ATR 347.

32 *Commissioner of Taxation v Multiflex Pty Ltd* (2011) 197 FCR 580.

33 ATO, *Decision Impact Statement - Commissioner of Taxation v Multiflex Pty Ltd*, 12 December 2011.

34 *Commissioner of Taxation v Multiflex Pty Ltd* (2011) 197 FCR 580, 581 at para 1.

35 ATO, above n 33.

36 Explanatory Memorandum, House of Representatives, Tax and Superannuation Laws Amendment (2012 Measures No. 1) Bill, 2012, p 2.

- (b) *the entity has requested the Commissioner to retain the amount for verification of the notified information, and the request has not been withdrawn.*<sup>37</sup>

2.25. In determining whether a refund should be retained, the Commissioner is required to consider 10 statutory factors:

- (1) *In deciding whether to retain the amount under this section, the Commissioner must, as far as the information available to the Commissioner at the time of making the decision reasonably allows, have regard to the following:*
  - (a) *the likely accuracy of the notified information;*
  - (b) *the likelihood that the notified information was affected by:*
    - (i) *fraud or evasion; or*
    - (ii) *intentional disregard of a taxation law; or*
    - (iii) *recklessness as to the operation of a taxation law;*
  - (c) *the impact of retaining the amount on the entity's financial position;*
  - (d) *whether retaining the amount is necessary for the protection of the revenue, including the likelihood that the Commissioner could recover any of the amount if the notified information were found to be incorrect after the amount had been refunded;*
  - (e) *any complexity that would be involved in verifying the notified information;*
  - (f) *the time for which the Commissioner has already retained the amount;*
  - (g) *what the Commissioner has already done to verify the notified information;*
  - (h) *whether the Commissioner has enough information to make an assessment relating to the amount (including information obtained from making further requests for information);*
  - (i) *the extent to which the notified information is consistent with information that the entity previously provided;*
  - (j) *any other relevant matter.*<sup>38</sup>

2.26. The ATO provides guidance to its officers on the operation of the above legislative provisions in its Law Administration Practice Statement PSLA 2012/6

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<sup>37</sup> Taxation Administration Act 1953 s 8AAZLGA(1).

<sup>38</sup> Taxation Administration Act 1953 s 8AAZLGA(2).

*Exercise of Commissioner's discretion to retain a refund* (PSLA 2012/6). There is also more general information on its refund verification process on its website.<sup>39</sup>

2.27. PSLA 2012/6 indicates that one of the above 10 factors may be sufficient to support a decision to retain the refund. Specifically, PSLA 2012/6 states:

*In some circumstances, and particularly where there is little information available to you, one factor alone might be sufficient to support a decision to retain the amount. However, in all cases you must consider each of the factors, and determine whether there is information available relevant to each one. You should then objectively consider each factor and determine whether it is reasonable in all the circumstances to retain the amount.*<sup>40</sup>

2.28. If the Commissioner decides to exercise his discretion, he must notify the taxpayer within certain prescribed timeframes from the lodgment date of a BAS:

- (1) *The Commissioner must inform the entity (by serving a document on the entity or by other means) that he or she has retained the amount under this section. He or she must do so by the end of:*
  - (a) *in a case to which paragraph 8AAZLF(1)(a) applies--the RBA interest day (within the meaning of section 12AF of the Taxation (Interest on Overpayments and Early Payments) Act 1983) for the RBA surplus of the entity; or*
  - (b) *in any other case--the 30th day after the entity gives to the Commissioner the notification mentioned in subsection (1) of this section.*<sup>41</sup>

2.29. The notification period does not commence until BAS lodgements are up to date as well as correct and complete bank details have been provided to the ATO. Where the taxpayer has outstanding BASs or where complete bank account details have not been provided, the Commissioner may retain GST refunds without needing to apply the requirements of section 8AAZLGA of the TAA 1953.

2.30. Failure to notify the taxpayer within the relevant period would require the ATO to pay the refund by the end of that period.<sup>42</sup> Once a decision has been made to retain a GST refund, the Commissioner may hold onto it until he considers it would no longer be reasonable to verify the information.<sup>43</sup>

2.31. PSLA 2012/6 also sets out the obligations of ATO officers under section 8AAZLGA of the TAA 1953 and expands upon certain timeframe requirements, such as when taxpayers are required to be notified of decisions to retain a refund.<sup>44</sup>

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<sup>39</sup> ATO, *Where is my BAS refund? - We check your refund* (18 April 2017) <<https://www.ato.gov.au>>.

<sup>40</sup> ATO, *Exercise of Commissioner's discretion to retain a refund*, PSLA 2012/6, 9 July 2016, appendix.

<sup>41</sup> *Taxation Administration Act 1953* s 8AAZLGA(3).

<sup>42</sup> *Taxation Administration Act 1953* s 8AAZLGA(5)(b).

<sup>43</sup> *Taxation Administration Act 1953* s 8AAZLGA(5)(a).

<sup>44</sup> ATO, *Commissioner's discretion to retain a refund*, above n 40, para 3.



Moreover, the PSLA also elaborates and expands on the matters that ATO officers are required to consider and provides illustrative examples for each of the 10 factors.<sup>45</sup>

2.32. The statutory factors are required to be reconsidered at appropriate times:

*[ATO officers] may only retain an amount until 'it would no longer be reasonable to require verification of the information'. This means that [officers] must reconsider whether the amount should be retained:*

- *Each time new information becomes available, or*
- *Circumstances change in a way that is relevant to [the ATO officer's] consideration of any of the 10 factors.*<sup>46</sup>

2.33. While the duration that the refund has already been retained is a factor to be considered, the guidance directs officers to review each retention decision by reference to the particular circumstances at that time. However, if nothing has changed, officers are not obliged to review the decision. In effect, the discretion to retain an amount is assessed on an ongoing basis.<sup>47</sup>

2.34. After notifying the taxpayer, the ATO has up to 60 days to retain a refund for verification before the taxpayer's right to object to the retention is triggered. However, this timeframe is extended where the Commissioner requests further information which was not previously provided to the ATO. Specifically, sub-section 14ZW(4) of the TAA 1953 states that:

*The 60 day period mentioned in subparagraph (1)(aad)(i) (including the period as extended by a previous application of this subsection) is extended by the number of days during that period in relation to which the following paragraphs apply:*

- (a) *on or before the day, but during the period, the Commissioner requests information from the entity for the purposes of verifying the notified information mentioned in section 8AAZLGA;*
- (b) *the Commissioner does not receive the requested information before the day.*

2.35. PSLA 2012/6 provides further guidance on the extension to the 60-day period, including circumstances where the extension mechanism does not apply.<sup>48</sup> It states:

*The 60-day period can be extended. This occurs when [ATO officers] request further information from the taxpayer. The extension covers the period of time between request and receipt of the requested information. For an extension to apply, the request for information must be made during the 60-day period (or the 60-day period as extended).*

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<sup>45</sup> ATO, *Commissioner's discretion to retain a refund*, above n 40, para 6 and appendix.

<sup>46</sup> Ibid, para 9.

<sup>47</sup> Ibid.

<sup>48</sup> Ibid, para 15.

*Any request for further information made within the initial statutory 14 or 30 day notification period does not extend the time after which an objection can be lodged.*

*The extension mechanism does not apply where it is necessary for [the ATO officer] to make requests of third parties (defined in footnote 11) for verification purposes.*

*If [ATO officers] make or amend an assessment that changes the entitlement to the amount, the taxpayer may object against the assessment or amended assessment under Part IVC.*



## CHAPTER 3 - THE ATO'S CASE SELECTION PROCESS FOR RETAINING GST REFUNDS FOR VERIFICATION PURPOSES

3.1. This chapter provides a broad overview of the ATO's risk-based case selection process and considers the effectiveness of this process in detecting incorrect or potentially fraudulent refund claims.

3.2. Annually, the ATO receives around 2.4 million BAS lodgments claiming credits and refunds. Approximately, 77 per cent are received electronically, while 23 per cent are paper lodgments.<sup>49</sup>

3.3. Given the nature of self-assessment, it is neither expected nor possible for the ATO to individually verify each BAS. Indeed, revenue authorities around the globe commit significant resources to information technology systems to minimise the need to manually review returns or BASs lodged. These systems generally comprise of risk assessment tools, and related data analytics, which identify cases that should undergo further examination, including manual checking.

3.4. Overall, the administration of GST refunds is operating efficiently with the vast majority of refunds processed and released promptly. Of the 2.4 million BASs lodged claiming GST refunds annually, the ATO's case selection process stops less than 1 per cent for verification, which represents less than 6 per cent of GST refund amounts claimed (approximately \$3 billion of a total of \$56.7 billion).<sup>50</sup>

3.5. The ATO's risk assessment tools drive the GST refund verification process. They distinguish those refunds that should be retained for further checking from those that should progress to payment. In doing so, they consider a number of factors including:

- the size of the refund being claimed;
- spikes in the value of the refund;
- changes in circumstances or behaviour; and
- attributes that indicate fraudulent activities may be taking place.<sup>51</sup>

3.6. The ATO has provided the IGT with detailed information on its risk assessment tools which are relevant to this review. However, the precise details and inner workings of these tools, including the thresholds and the data inputs used by the ATO, are not disclosed in this report in order to maintain the integrity of the system.

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49 ATO, 'Refund Integrity Case Selection Process', internal ATO document, 26 July 2017.

50 ATO, 'Overall Pre-Issue Refund Integrity Case Outcomes by Age', internal ATO document.

51 ATO, *Where is my BAS refund?*, above n 39.

## STAKEHOLDER CONCERNS

3.7. Stakeholders have acknowledged that the ATO bears significant responsibility in receiving and processing millions of BASs and GST refunds each year and that the process generally operates well. Additionally, they have positively reflected on the ATO's commitment to improve its processes and to receive feedback through channels such as its GST Stewardship Committee.

3.8. However, some stakeholders have questioned the effectiveness of the ATO's risk assessment tools. They believe that certain valid refunds are retained whilst others, which warrant a more thorough verification process, progress to payment without being stopped. These concerns are supported by ATO performance reports which suggest that the risk assessment tools achieve a strike rate as low as 1:4 or 1:5,<sup>52</sup> that is, only one in four or five refunds that are stopped ultimately result in any adjustment.

3.9. The low strike rate has been attributed to the risk assessment tools being over reliant on the net GST refunds without an appropriate consideration of other factors, which may be deduced from the BAS itself, such as the nature of the relevant activities and transactions as well as the taxpayer's overall compliance history.

3.10. The unnecessary retention of refunds adversely impacts the cash flow of affected taxpayers, particularly small businesses. This is further explored in Chapter 5.

## ATO MATERIALS

### Overview of the ATO's GST refund integrity process

3.11. Broadly, the ATO's risk assessment system uses BASs as input data and automatically selects a number of cases where retention of refund and further checking should be considered. The selection is then further refined by manual intervention.

3.12. Specifically, the risk assessment system consists of two parallel processes as depicted in Figure 3. The two processes commence with distinct automated case selection processes namely the:

- Risk Rating Engine (RRE); and
- Suspect Refund (SR) models.

3.13. The output from the RRE undergoes further automated filtering whilst the SR models selection is subjected to manual filtering.<sup>53</sup>

3.14. In cases that are ultimately classified as high risk by either process, refunds are retained for pre-issue verification. Where cases are classified as high risk by both processes, the ATO officer actioning the outcome of the processes, which commenced

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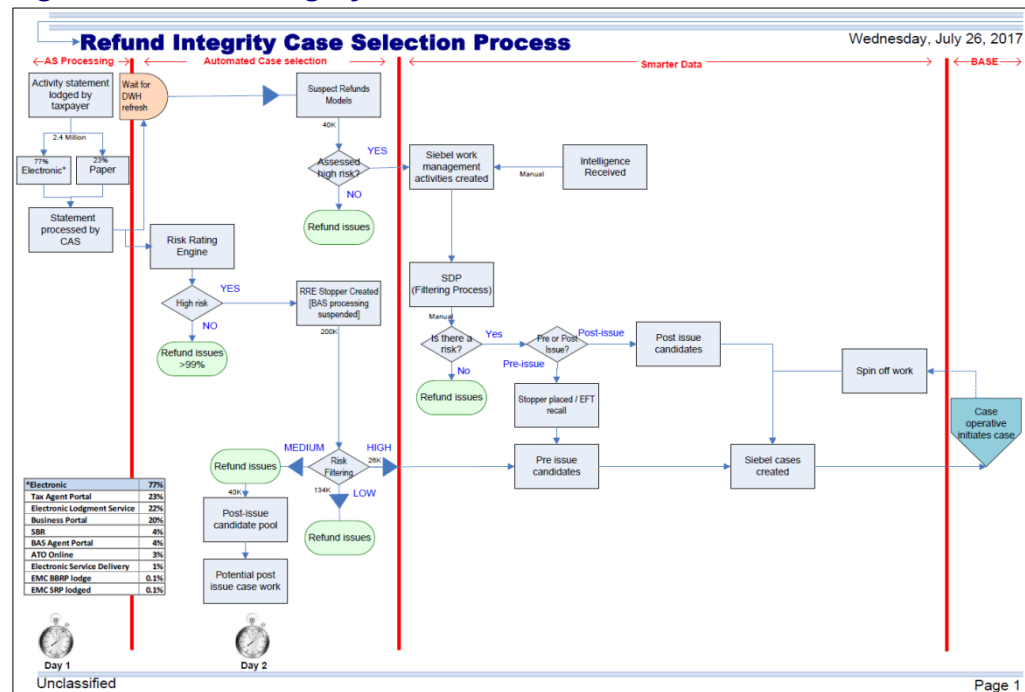
<sup>52</sup> ATO, *GST administration annual performance report 2015–16*, (20 April 2017) p 35.

<sup>53</sup> ATO, 'RI Auditor Guide', internal ATO document, p 60.

with RRE, is notified of the risks identified by the other process and that officer, then, acts on the information obtained from both processes.<sup>54</sup>

3.15. In the event that a case is classified as low risk by both processes, the refund is issued immediately without further checking. Where the highest risk category attributed to a case by either processes is medium risk, the refund is also issued immediately but the case is flagged for potential post-issue audit action.

**Figure 3: Refund Integrity Case Selection Process**



Source: ATO

3.16. The pre-issue verification cases are allocated to ATO case officers and actioned as reviews in most instances but may also be escalated to audit. Standardised case context documents (CCD) are produced as a result of the above risk filtering and are automatically linked to the relevant review or audit activities. The CCD includes reasons why the case was created, the risks that have been identified and the corrective action needed.<sup>55</sup>

## The ATO's automated risk assessment tools

### Risk rating engine (RRE)

3.17. The ATO has advised that the RRE was the first risk model implemented following the introduction of GST in 2000 and has since undergone several

<sup>54</sup> ATO, 'RI Auditor Guide', above n 53, p 60.

<sup>55</sup> ATO, 'ITX Case Context Document: Review – Pre/Post Issue Refund Integrity Risk', internal ATO document (June 2015), p 2.

enhancements. It comprises a set of systems-based rules which process BAS lodgments in real time.<sup>56</sup>

3.18. The inputs to the RRE include taxpayer and transaction data such as:

- Registration details;
- Lodgment history for both income tax returns and business activity statements;
- Compliance history and indicators;
- Geographical profile;
- AUSTRAC, Auskey and bank details;
- Activity statement benchmarks and ratios; and
- Linked entities.<sup>57</sup>

3.19. The RRE uses the above inputs, as well as the amount of the refund being claimed, to identify refund cases that may pose certain risks having regard to the underlying transactional data.

3.20. More fulsome descriptions of the RRE rules are provided to ATO case officers to understand the context of the risks that the ATO is seeking to address and the reasons for the selection of a particular BAS or taxpayer for a review. In addition to the high level summary of risks factors considered by the ATO, examples are provided on the ATO website of when a refund may be selected for review.<sup>58</sup> As noted previously, it would be undesirable for the IGT to disclose further details on the inner workings of these models.

### **Suspect refund models (SR)**

3.21. The SR models were created to address high risk refunds cases, in response to the higher volume, low value refunds that circumvented RRE identification.<sup>59</sup> They are primarily focused on risks of fraudulent behaviour including potential:

- identity fraud;
- links to fraud risk groups; or
- anomalous reporting patterns.

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<sup>56</sup> ATO, 'RI Auditor Guide', above n 53, p 60.

<sup>57</sup> ATO, 'Analytical filter model for NRRE', internal ATO document (June 2015), pp 1-2.

<sup>58</sup> ATO, *Where is my BAS refund?*, above n 39.

<sup>59</sup> ATO, 'The GST Refund Risk - presentation to Indonesian Delegation', internal ATO document (October 2016), slide 8.

3.22. The case selection for the SR models are batch processed, the output from which is also subject to additional manual officer 'profiling' to filter out cases that do not present a risk.<sup>60</sup> Unlike the RRE, the SR process requires an ATO officer to put a manual stop on the system to prevent the GST refund from being processed and issued.<sup>61</sup> If the manual filtering indicates that a high but not immediate risk exists then the case is classified as medium risk. Notes are recorded by ATO officers performing the manual filtering on each of the SR cases requiring further action.

3.23. As with the RRE rules, ATO officers who are responsible for actioning the case are provided with further details on the reasons for selection of a particular BAS or taxpayer for review. In line with the IGT's earlier comments, further disclosure of the underlying inputs and operation of the SR models may compromise the integrity of the system.

### **Other automated risk assessment tools**

3.24. The ATO also uses a number of other automated risk assessment tools, predominantly Expert Business Rules (EBRs) which target specific fraud risks. These rules augment the work done by the SR models and consider precise attributes in order to detect high risk refunds or entity registrations. The EBRs and the SR models are processed independently and a hierarchy of the risk models determines which risks take priority and how the case is to be considered for reporting purposes. As only one reason for case selection is recorded in the system, case officers need to be aware that other risks may also be at play.<sup>62</sup>

### **Effectiveness of the GST refund integrity process**

3.25. The Outcome Effective Strike Rate (OESR) and the Actual Strike Rate (ASR) are two measures that indicate the effectiveness of the ATO's automated and manual risk assessment processes. They express the percentage of selected cases that ultimately result in adjustments to net GST positions against total cases selected by each process.<sup>63</sup> The OESR considers the number of outcomes achieved in all cases whereas the ASR considers only audit outcomes over the number of audit cases.

3.26. A summary of the strike rates for the 2015-16 and 2016-17 financial years are set out in Tables 1a and 1b below.

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60 ATO, Communication to the IGT, 27 June 2017.

61 ATO, 'RI Auditor Guide', above n 53, p 60.

62 ATO, 'ITX Case Context Document', above n 55, p 4.

63 ATO, ITX RIS Model Performance 2015-16, internal ATO document.

**Table 1a: Pre-issue verification cases completed in the 2015-16 financial year**

Model	Total cases	Total audits	Reviews escalated to audit	Audit outcomes	Total outcomes	OESR	ASR
RRE	15,856	3,593	3,650	2,136	2,245	18.4%	59.4%
SR	10,825	3,861	3,446	2,451	2,519	34.1%	63.5%
Other	774	501	136	322	326	51.1%	64.3%
<b>TOTAL</b>	<b>27,455</b>	<b>7,955</b>	<b>7,232</b>	<b>4,909</b>	<b>5,090</b>	<b>25.2%</b>	<b>61.7%</b>

Source: IGT constructed from ATO information.

Note 1: Total cases comprises both Review cases (19,500) and Audit cases (7,955).

Note 2: The OESR is calculated by dividing total outcomes by total cases less reviews escalated to audit. This is necessary to avoid double counting cases that may have subject to both a review and an audit.

Note 3: The ASR is calculated by dividing audit outcomes by total audits.

Note 4: Full source data including further notes are included in Appendix 2.

**Table 1b: Pre-issue verification cases completed in the 2016-17 financial year**

Model	Total cases	Total audits	Reviews escalated to audit	Audit outcomes	Total outcomes	OESR	ASR
RRE	13,614	3,084	3,113	1,904	2,016	19.2%	61.7%
SR	9,134	3,113	2,932	2,134	2,216	35.7%	68.6%
Other	565	444	60	366	369	73.1%	82.4%
<b>TOTAL</b>	<b>23,313</b>	<b>6,641</b>	<b>6,105</b>	<b>4,404</b>	<b>4,601</b>	<b>26.7%</b>	<b>66.3%</b>

Source: IGT constructed from ATO information.

Note 1: Total cases comprises both Review cases (16,672) and Audit cases (6,641).

Note 2: The OESR is calculated by dividing total outcomes by total cases less reviews escalated to audit. This is necessary to avoid double counting cases that may have subject to both a review and an audit.

Note 3: The ASR is calculated by dividing audit outcomes by total audits.

Note 4: Full source data including further notes are included in Appendix 2.

3.27. Table 1a indicates that in the 2015-16 financial year, the ATO's automated risk assessment tools selected a total of 27,455 cases for verification. After manual and other risk filtering, which may include contact with taxpayers, the number of cases that proceeded to audit was 7,955 and, of those, only 5,090 required any adjustment to net GST positions. It shows a total OESR of 25.2 per cent meaning that of all the cases selected by the ATO's automated risk assessment tools, 1 in 4 resulted in adjustments.<sup>64</sup>

3.28. However, the ASR is considerably higher at 61.7 per cent suggesting that performance was significantly improved following manual and other risk filtering.

3.29. Table 1a also shows the performance of each of the automated risk assessment tools, namely the RRE, SR and the other models, for the 2015-16 financial year. For example, the OESR and ASR for those cases selected by the RRE were 18.4 per cent and 59.4 per cent respectively. These figures provide insight on how each element of the automated risk assessment tools performs in isolation. They suggest that the EBRs (shown as 'Other' in above tables) and the SR models generally perform better than the RRE with and without additional manual and other risk filtering.

<sup>64</sup> Other statistics provided to the IGT as part of broader project work suggest that the 2015-16 'outcome effective strike rate' was 24.8 per cent due to an uplift in performance as a result of model enhancement: Client Engagement Risk Investment (undated). See also: ATO, ITX RIS Model Performance 2015-16, internal ATO document (Appendix 2).

3.30. In the 2016-17 financial year, the performance of the ATO's automated risk assessment tools improved, both at an overall level and in respect of each of the RRE, SR and other models. As set out in Table 1b, the ATO's risk assessment tools selected fewer potential cases requiring verification and following manual and other risk filtering, only 6,641 were selected for audit. The overall OESR and ASR were 26.7 per cent and 66.3 per cent for that year, respectively. A more detailed breakdown of the performance of these tools is contained in Appendix 2.<sup>65</sup>

3.31. The ATO measures its strike rate performance against a range of internal benchmarks, having regard to the resources available that year. Table 2 sets out the ATO's benchmark strike rate for each of the financial years from 2013-14 to 2016-17 (inclusive) as well as the numbers of full time equivalent (FTE) employees and review or audit cases planned.

**Table 2: High level summary risk plans for GST refunds**

Planned targets	2013-14	2014-15	2015-16	2016-17
FTEs	253	231	216	188
Review cases	3,393	21,994	21,340	17,069
Escalation rate	6%	57%	43%	42%
Audits	23,404	14,037	10,549	8,902
Actual Strike Rate	36%	53%	53%	59%

Source: IGT constructed from ATO information.

Note: In the 2013-14 year, the ATO introduced 'review cases' to the GST retention work and as such, it represented a significantly lower proportion of cases when compared with subsequent years. FTE figures have also been rounded.

3.32. Table 2 indicates that the ATO had planned to improve its strike rate but decrease its numbers of FTEs, from 253 in 2013-14 to 188 in 2016-17, and its review and audit cases.

3.25. Table 3 sets out the ATO's actual performance in terms of OESR and ASR for each of the financial years between 2013-14 and 2016-17.<sup>66</sup> However, the ATO has not provided the actual number of FTEs for these years.

**Table 3: Pre-issue strike rates for GST reviews and audits**

Actuals	2013-14	2014-15	2015-16	2016-17
Reviews	3,210	24,101	19,500	16,672
Audits	21,811	9,249	7,955	6,641
Escalations	284	8,485	7,232	6,105
Review adjustments	43	328	181	197
Audit adjustments	5,723	4,951	4,909	4,404
Outcome Effective Strike Rate	23.3%	21.2%	25.2%	26.7%
Actual Strike Rate	26.2%	53.5%	61.7%	66.3%

Source: ATO

3.34. Comparing Tables 2 and 3 suggests that the ATO met or exceeded its planned strike rate in every year with the exception of the 2013-14 financial year. The ATO believes that the higher strike rates are attributable to the enhancements of the RRE

<sup>65</sup> ATO, ITX RIS Model Performance 2015-16, internal ATO document.

<sup>66</sup> ATO, above n 50.



and improvement of staff capabilities resulting in reduced audit escalations, complemented with the introduction of a less intensive review of lower risk cases which did not warrant full audits. The ATO has also noted that as a result of improvements from a project initiated by the Client Engagement Risk Investment Committee (CERIC Project), it had seen an increase in its OESR performance. For example, it has noted that the OESR for the 2016-17 financial year had increased from 23.8 per cent in the first quarter to 26.7 per cent by the end of the year.<sup>67</sup>

3.35. At a broader level, the ATO also reports its performance for GST compliance activities based upon the levels of liabilities adjusted or 'revenue protected'. In the 2015-16 financial year, the ATO reported that as a result of its pre-issue verification activities, it disallowed \$490 million in refund claims, which represents approximately 10 per cent of the total refund amount retained for verification (\$5 billion).<sup>68</sup>

3.36. It should be noted that the ATO applies a *de minimis* policy to finalise cases without adjustment where any proposed adjustment falls under a particular monetary threshold.<sup>69</sup> These cases are treated as having a 'nil outcome' allowing the refund amount to issue as the administrative costs of amending the assessment outweighs the benefits. In these cases, the ATO provides education to the taxpayer by explaining the error and the potential consequences if similar errors are made in future.<sup>70</sup>

## Improvement to the risk assessment tools

3.37. The ATO seeks to improve the effectiveness of its automated risk assessment tools through feedback received after the completion of the verification process.

3.38. Following the verification process, ATO officers are required to record any emerging patterns or attributes on a form called the Case Data Capture (CDC) form.<sup>71</sup> Data from the CDC is used as feedback and incorporated into the SR models, EBRs and risk filtering tools to better detect potential risks such as criminal links, sham arrangements and unreported sales.

3.39. In addition to the CDC form, the ATO encourages its officers to record less critical intelligence, which may have been gathered from their cases, on its corporate database, ATOintelligence Discover (ATOi). Information recorded on ATOi is considered by the ATO's Smarter Data business line to identify industry specific risks, increases in unusual behaviours, complex transactions between associated taxpayers and new schemes.<sup>72</sup> The intelligence gathered by the Smarter Data business line is used by the ITX business line as part of its broader risk and audit strategies.

3.40. The ATO has also advised that its Refund Integrity Strategy team, within the ITX business line, conducts face-to-face discussions with its case officers twice a year to

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67 ATO, above n 50; ATO, Client Engagement Risk Investment – GST Refund Integrity Risk, internal ATO document.

68 ATO, above n 50.

69 ATO, Small errors policy, internal ATO document (6 September 2016).

70 Ibid.

71 ATO, 'RI Auditor Guide', above n 53, p 128 and 150.

72 Ibid, pp 211–212.



discuss GST refund risks.<sup>73</sup> The purpose of these discussions is to provide training to ATO officers regarding systems and processes, raise awareness of the particular risks that the risk assessment tools are seeking to address and to reinforce the importance of feedback loops.<sup>74</sup>

3.41. One of the challenges that the ATO has identified with its feedback loops is the inconsistency with which officers provide feedback through discussions or documentation such as the CDC form. For example, in certain ATO teams, fewer than half of finalised cases result in a CDC form being completed.<sup>75</sup>

3.42. In addition to the feedback loops, the ATO undertakes internal reviews of its systems and processes. In 2015, the ATO conducted a small random audit program focusing on 497 taxpayers across five industries that had claimed over \$1,000 in GST refunds. The program found that 'strike rates recorded by the random sample are almost equivalent to that achieved through risk based selection strategies.'<sup>76</sup> However, the ATO found that the amount of the amendments was on average much greater under risk based selection.<sup>77</sup> The CERIC Project, mentioned above, made similar findings in relation to the strike rates of automated risk assessment tools:

*Within the total suite of candidate selection models, certain 'Expert Business Rules' recorded rates of escalation comparable to what could be achieved by random selection. Candidate selection models had been developed without supporting documentation, making it all but impossible to properly assess output populations. And the logic underpinning the candidate selection models was largely event driven, reflecting an out-dated understanding of fraud.*<sup>78</sup>

and

*That analysis identified that the entire suite of candidate selection models and the logic underpinning those models were performing very poorly. In addition to identifying a very poor rate of effectiveness, measured by calculating the rate of escalation from initial candidate identification (Pre-Issue Review) to audit (and audit result), the review also demonstrated a very poor 'revenue raised' outcome.*<sup>79</sup>

3.43. Following the above finding, the ATO discontinued 22 EBRs and redesigned 10 new SR models.<sup>80</sup> The ATO has advised that whilst 22 EBRs were discontinued, new rules have been developed and are currently being tested prior to deployment.<sup>81</sup>

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<sup>73</sup> ATO, Communication to the IGT, 27 June 2017.

<sup>74</sup> ATO, 'Indirect Tax Executive Submission Paper - 2017 RIS/ BASE Risk Presentation' (24 March 2017) internal ATO document.

<sup>75</sup> ATO internal email, 20 June 2016.

<sup>76</sup> ATO, 'Refund Integrity Random Audit Program Results' (2015), internal ATO document, p 3.

<sup>77</sup> Ibid.

<sup>78</sup> ATO, 'CERIC Report' (2016), internal ATO document p 1.

<sup>79</sup> Ibid.

<sup>80</sup> Ibid, p 2.

<sup>81</sup> ATO, 'The New nRRE Filter Model' (1 August 2017) internal ATO document; ATO, 'Performance comparison of the new and old hybrid models - updated with the most recent data since the new model was deployed (20170802)', internal ATO document (1 December 2017).

3.44. The CERIC Project also revealed that the manual risk filtering within the SR case selection process required improvement:

*Most notably, manual profiling was undertaken on 100% of the model outputs irrespective of total volumes and during peak lodgment periods, very large volumes of candidates are generated. Excessive workloads contribute to poorly considered profiling decisions.*

*The absence of a feedback loop has meant that case outcomes (and by extension profiling decision) were not relayed back to the profiling team. Profiler's decision making logic is drawn entirely from audit experience and lacks fundamental intelligence principles.*

*Additionally, the profiling function was rotated between audit teams, each spending a six month period performing the profiling function before returning to their audit role. The overall effect was that a profiler's decision making lacked transparency and consistency. With little or no post selection analysis, no feedback and a floating workforce it was impossible to ensure consistent decision making.<sup>82</sup>*

3.45. More broadly, the CERIC Project characterised the GST refund verification process as 'resource intensive'.<sup>83</sup> The ATO deployed 312 FTEs to manage GST refund risks across multiple business lines,<sup>84</sup> including 9 FTEs allocated to the manual filtering process. The number of FTEs allocated to GST refund verification work has decreased in subsequent years which the ATO attributes to improvements in the risk assessment tools. According to the ATO's annual performance report, compliance costs as a proportion of total GST administration costs have remained relatively steady at 51 per cent.<sup>85</sup>

3.46. In addition to the CERIC Project, in 2016, the ATO undertook a Business Improvement Review (BIR) to assess 'the effectiveness of the ATO's existing processes for the management of refund fraud'.<sup>86</sup> It noted that:

*[Internal ATO] stakeholders consistently describe the quality of fraud data – especially refund fraud data – as poor. Data collection systems do not currently support enterprise-level capture of meaningful, coherent metrics on refund fraud.<sup>87</sup>*

3.47. A key issue raised in the BIR, regarding the identification of GST refund fraud, was:

*Data on [GST] refund fraud currently sits across a myriad of automated models, systems and manual databases that are managed within business lines and branches. These data sources operate independently of each other and are not readily accessible to users outside of the business area that*

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82 ATO, 'CERIC Report', above n 78, p 3.

83 ATO, 'Client Engagement Risk Investment – GST Refund Integrity Risk', internal ATO document.

84 Ibid.

85 ATO, *GST administration annual performance report*, above n 52, p 6.

86 ATO, 'Business Improvement Review - Management of Refund Fraud in the ATO' (2017), internal ATO document.

87 Ibid, p 25.

*'owns' the data. The dataset provided by one system is generally not compatible with the dataset provided by another (that is, apples and oranges).*

*Where accurate and relevant refund fraud data is not available, the practice has been to extract whatever data is available and massage that data into a form that may go close to meeting the requirement.*

*The review team found that the disparate nature of the mechanisms that capture refund fraud data severely limits the ATO's ability to compile accurate, defensible whole-of-agency reporting that meets internal and external requirements. This is compounded by the reality that existing refund integrity reporting systems do not distinguish between refund fraud and refund integrity issues.*

*Refund fraud data is therefore included in broader refund integrity performance data and, at present, cannot be separated. This situation is likely to have resulted in unintentional misreporting.<sup>88</sup>*

3.48. During this review the ATO has also advised the IGT that, at the time taxpayers lodge their BASs, the quality of the data inputs available to the ATO, is one of the main barriers to improving the accuracy of its risk assessment tools.<sup>89</sup> The ATO has noted that with the introduction of Simpler BAS for small businesses commencing on 1 July 2017, the need for better data has become increasingly important. The availability of high quality data for use in the ATO's risk assessment tools has been broadly considered in previous IGT reviews.<sup>90</sup>

3.49. Simpler BAS seeks to reduce compliance costs for small businesses by requiring fewer BAS labels to be completed, making less information available to the ATO's risk assessment tools.<sup>91</sup> The ATO has explored alternative means of estimating the same information by using the information contained in the remaining labels.<sup>92</sup>

3.50. In addition to drawing information from the remaining BAS labels, the ATO undertakes data mining to extract trends and other key attributes that may signify non-compliance.

## On-line BAS Check Tool

3.51. The ATO has advised the IGT that a large proportion of BASs stopped for verification are due to avoidable errors such as incomplete labels or incorrect bank

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<sup>88</sup> ATO, 'Business Improvement Review', above n 86, p 16.

<sup>89</sup> ATO, Communications to the IGT, 10 October 2017 & 16 October 2017.

<sup>90</sup> IGT, *Review into the Australian Taxation Office's compliance approach to individual taxpayers – use of data matching* (2013); IGT, *Review into Aspects of the Australian Taxation Office's Use of Compliance Risk Assessment Tools* (2013).

<sup>91</sup> ATO, *Changes to ATO processes to support Simpler BAS transition* (30 June 2017) <<https://www.ato.gov.au/>>.

<sup>92</sup> ATO, 'Simpler BAS Proxies – Analysis of possible substitutes for GST labels in risk models impacted by Simpler BAS' (2017), internal ATO document.

account details on BASs. The ATO has identified that these types of errors account for approximately 57 per cent of adjustments in refund verification cases.<sup>93</sup>

3.52. The ATO has proposed implementing an On-line BAS Check tool (OBC tool) as a preventative measure to reduce these types of errors in real time. The OBC tool supports the ATO's anticipated decline in FTEs available to undertake refund verification work. It operates in a similar manner to those in existing online systems, such as myTax, where the system alerts taxpayers to errors identified in their lodgment.<sup>94</sup> The benefits of this tool have been reported as:

*BAS Validation through the Online BAS Check will provide assurance to businesses as part of their pre-lodgment that their BAS is correct and within reasonable parameters. Identifying potential errors at this point is expected to reduce approximately 57% of audit cases where simple errors have been made. This will save significant resource and better align the completion of a client's taxation obligations to their natural business systems.*<sup>95</sup>

3.53. While the OBC tool prompts the user or taxpayer to correct the error (for example, revising their bank account details or relevant fields), it does not prevent lodgement if the error is not rectified.

3.54. The OBC tool has already been developed and incorporated into myGov for individuals and sole traders. The ATO is also seeking to expand the basic tests that comprise the OBC tool and is expecting it to be implemented on other on-line platforms such as the ATO Portals to prevent mistakes prior to lodgment. However, further deployment of the OBC tool is dependent upon appropriate testing being conducted which, in turn, is dependent upon resourcing being available in other areas of the ATO, such as the Enterprise Solutions and Technology business line. The ATO has tentatively planned for its deployment in either 2017-18 or 2018-19.<sup>96</sup>

## IGT OBSERVATIONS

3.55. The IGT, as well as all stakeholders acknowledge the ATO needs to strike a balance between maintaining the integrity of the GST system and the prompt issuing of refunds to taxpayers. The IGT also appreciates that in modern tax administration, a risk based approach, with appropriate use of technology, has to be adopted and complemented by manual processing where necessary.

3.56. As discussed above, the analysis of the raw performance statistics that the ATO has provided to the IGT during this review, indicates that there has been general improvement in the ASR during the four financial years from 2013-14 to 2016-17 from 26.2 per cent to 66.3 per cent. During the same period, with the exception of the 2014-15 financial year, the OESRs have also improved increasing from 23.3 per cent to 26.7 per cent.<sup>97</sup> Notwithstanding the improvements, the OESRs suggest that

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93 ATO, 'Client Engagement Risk Investment', above n 83.

94 Ibid.

95 Ibid.

96 ATO, 'On-Line BAS Check Project' (7 August 2017), internal ATO document.

97 ATO, above n 50.

approximately 75 per cent of cases selected for pre-issue verification are ultimately released without any adjustment.

3.57. Whilst any risk assessment tool cannot be 100 per cent accurate, particularly if they are automated processes, there are opportunities for improvements if they only achieve an accuracy rate of 26.7 per cent – the ATO's own review found that at least part of the risk assessment systems yielded results no better than random selection,<sup>98</sup> albeit that average amount of the amendments were found to be higher under risk-based selection. Notwithstanding higher average amendments amounts, such low levels of accuracy place a greater strain on the ATO resources, that is, greater need for manual processing, at a time when the ATO is decreasing its staffing in this area. It may also cause unnecessary delay in issuing refunds to compliant taxpayers, adversely impacting their cash flows and increasing their compliance burden.

3.58. The high level of BASs selected by the ATO's automated risk assessment tools that are subsequently released without adjustment may also raise concerns that they are not adequately detecting fraudulent, overstated or mistaken claims for refund. However, it could also be argued that, given approximately 75 per cent of cases selected do not result in any adjustments, the automated tools are sufficiently, if not overly, sensitive to such refund claims.

3.59. The IGT acknowledges that the overall ATO strike rate improved in 2016-17 following internal reviews and subsequent implementation of the outcome of those reviews. However, as mentioned above, further improvements are necessary. Moreover, as fraudulent behaviour adapts and modifies over time, the ATO's risk assessment tools need to keep pace. Reviews need to be undertaken periodically as part of a broader framework of continuous improvement.

3.60. Periodic reviews should be conducted with fulsome evidence and intelligence provided by officers operating at the coalface. Based on the information provided by the ATO, there is an opportunity to improve the collection of such data from these officers, whether through existing channels such as the CDC forms and ATOi or on other platforms that the ATO may seek to develop in future. Intelligence capture should also be improved through greater engagement between risk managers and operational teams across different business lines such as ITX and Smarter Data.

3.61. Enhancements and improvements of the risk assessment tools should also be informed by robust performance reporting. Whilst large amounts of raw data were made available to the IGT during this review, there appeared to be limited analysis of this data for the individual models resulting in minimal reporting both within the ITX business line and to the ATO Executive Committees. Consistent and robust performance reporting are particularly important in ensuring that decision makers are fully informed of areas that are performing well and those that need refinement or overhaul.

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98 ATO, 'CERIC Report', above n 78, p 1.

3.62. The framework of continuous improvement proposed above aligns with recommendations in a previous IGT review, namely: the *Review into aspects of the ATO's use of compliance risk assessment tools*.<sup>99</sup> Recommendations 3.8 and 4.1 of that review are particularly relevant. Although these recommendations were directed at large business risk identification processes, they nonetheless encouraged more engagement between risk managers and operational teams, improving data capture, refining or removing inappropriate risk filters and incorporating ATO officer experience and case outcomes as part of the review process. Furthermore, the ATO should also consider recommendation 8.1 and the checklist contained in Appendix 12 of that review in the development or improvement of its risk assessment tools.

3.63. As an ancillary issue, the IGT is of the view that the large proportion of adjustments, which the ATO believes are due to avoidable errors made in completing BASs, should also be addressed. To the extent that the OBC tool addresses this issue adequately, its deployment should be prioritised.

### RECOMMENDATION 3.1

*The IGT recommends that the ATO:*

- (a) *develop a formal framework of continuous improvement for its risk assessment tools which includes:*
  - (i) *periodic reviews with clear milestones;*
  - (ii) *ensuring that case officers are consistent and accurate in reporting case related data and other pertinent matters in all relevant cases;*
  - (iii) *improving intelligence capture through greater engagement between risk managers and operational teams across different business lines such as Indirect Tax and Smarter Data;*
  - (iv) *developing a suite of performance reports for use within the Indirect Tax business line and ATO Executive Committees; and*
- (b) *prioritise the deployment of the On-Line BAS Check tool.*

### ATO RESPONSE

#### (a) Agree

The ATO agrees that a robust, well documented framework to continually review and assess our risk assessment tools is important for continuous improvement.

In relation to subparagraph (i) of this recommendation, the ATO already undertakes regular reviews of its risk assessment models and as acknowledged in the report, there has been continuous improvement in the ATO's ability to detect incorrect refund Business Activity Statements (BAS) while reducing the number of taxpayers impacted.

In relation to subparagraph (ii) of this recommendation, the ATO has recently updated its Case Data Capture (CDC) form in consultation with the Risk Manager and Smarter Data to ensure relevant information from compliance cases is more accurately captured. The CDC form has been structured so that the information submitted by case

<sup>99</sup> IGT, 'Compliance Risk Assessment Tools', above 90.



officers is consistent and accurate, focusing on reasons for the decision and taxpayer behaviours via relevant drop down options.

In relation to subparagraph (iii) of this recommendation, the ATO will look at ways to further improve intelligence gathering and greater engagement between risk managers, Smarter Data and operational staff.

**(b) Agree**

The Online BAS Check (OBC) has been endorsed by the Strategy and Integration Committee. The project is in Delivery Planning and is due for release in the 2018/19 year.





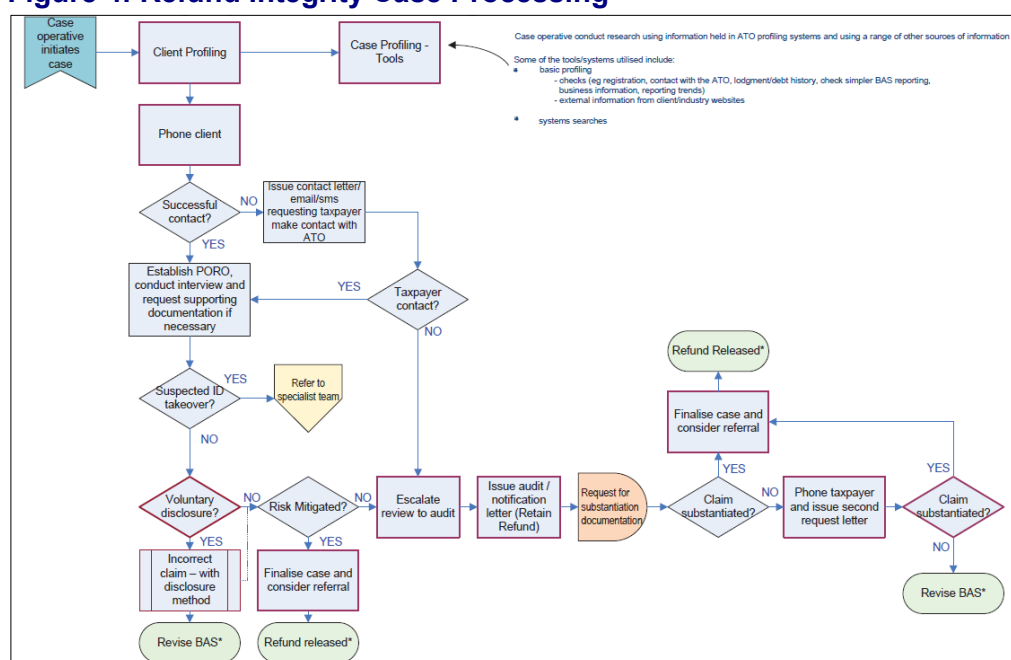
## CHAPTER 4 - ENGAGEMENT WITH TAXPAYERS AND TAX PRACTITIONERS DURING GST REFUND VERIFICATION

4.1. This chapter examines the ATO's processing of GST refund cases which have been identified for pre-issue verification. In particular, it will explore how the ATO engages with taxpayers and tax practitioners throughout this process as such engagement is of overarching importance to the efficiency of the pre-issue audits.

### OVERVIEW OF THE ATO'S PRE-ISSUE AUDITS

4.2. Once a case has been selected for pre-issue verification (as set out in Chapter 3), the case is generally allocated to an officer in the BAS Engagement (BASE) teams although a small number of cases may be referred to officers in Public Groups Assurance and Engagement (PGE). The process followed by officers in BASE teams is depicted in Figure 4, below, and is known as Refund Integrity Case Processing (RICP). A number of procedures and guidelines are available to assist and support such officers in managing this process.

**Figure 4: Refund Integrity Case Processing**



Source: ATO

4.3. The RICP is made up of two compliance processes, namely, the review and audit phases. In Figure 4, stages from 'Case operative initiates case' to the 'Escalate Review to Audit' represent the review phase. The actions that take place in the review phase usually occur within the first 14 days after the BAS is lodged. Importantly, the ATO is empowered to retain any GST refund, without any restriction during this period.

4.4. During the review phase, ATO officers consider whether it would be appropriate to 'early exit' the case, that is, take no further action. The ATO's Refund Integrity (RI) Auditor Guide, the primary source of instruction for ATO officers undertaking pre-issue verification work, sets out the circumstances in which it may be appropriate to do so. These circumstances include situations where:

- compliance action has already commenced relating to the same or similar risks;
- the taxpayer is deceased or insolvent. [ATO officers] should appropriately assess the taxpayer to ensure genuine insolvency exists and the CAC [Client Account Centre] under review must have the INS (insolvency) indicator if [the officer] intends to consider early exit for this reason;
- the case was incorrectly selected or is a duplicate case;
- the case was created using the incorrect case product; and
- the [particular compliance] project has ceased.<sup>100</sup>

4.5. If an ATO officer decides not to 'early exit' the case, it is moved to the next stage, 'Client Profiling'. At this stage, ATO officers are required to understand the taxpayers and their business environments in preparation for any engagement with them. It involves ATO officers obtaining and verifying information, including information which may be held by other government or private organisations. Some of the tools which are available to ATO officers for this task include:<sup>101</sup>

- internal ATO systems such as the BAS Analyser and Risk Assessment Profiling Tool (RAPT); and
- external systems such as Mirrored Australian Securities Commission On Time (MASCOT) and Real Property (RP) Data.

4.6. Once 'Client Profiling' is completed, the case moves to the 'Phone Client' stage. No direct taxpayer engagement needs to occur before the latter stage. The ATO expects its officers to contact taxpayers within forty-eight hours to advise them that their GST refund has been selected for review and to outline the ATO's verification process.<sup>102</sup> Officers are encouraged to contact taxpayers by telephone in the first instance. If successful, during the initial telephone conversation, officers are required to gather further information to better understand the taxpayer's business, clarify and determine the risks identified by ATO risk assessment tools and, where necessary, request documents to substantiate the claim.<sup>103</sup> Where telephone contact is unsuccessful, written correspondence is issued via email or post.

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<sup>100</sup> ATO, 'RI Auditor Guide', above n 53, p 79.

<sup>101</sup> Ibid pp 82-107.

<sup>102</sup> ATO, 'ITX Review Streamlined', internal ATO document, p 5.

<sup>103</sup> ATO, 'RI Auditor Guide', above n 53, p 119.

4.7. After reviewing information provided by the taxpayer and verifying it against third party data and information accessed from the ATO systems, the officer determines whether the risks identified have been mitigated or whether the claim requires further verification.<sup>104</sup>

4.8. Where further verification is required, the ATO officer must decide whether to exercise the Commissioner's discretion to retain the refund under section 8AAZLGA of the TAA 1953.<sup>105</sup> The decision is made in accordance with guidance contained in PSLA 2012/6<sup>106</sup> as well as the RI Auditor Guide and a set of 'Frequently Asked Questions' that have been developed by the ATO (internal FAQs).<sup>107</sup>

4.9. As part of their decision making, ATO officers are required to consider and document their consideration of the 10 statutory factors outlined earlier<sup>108</sup> by completing a template or an appropriate file note and store it on the Siebel system.<sup>109</sup> The ATO has developed two templates, being a Word document and an Excel worksheet, for officers to use. While ATO officers are required to consider each of the 10 statutory factors there may be situations where it is not possible to do so due to insufficient information being available.<sup>110</sup>

4.10. Decisions to retain a refund generally need to be approved by technical or team leaders. However, if ATO officers making the decision are 'Accredited Officers', no such approval is necessary provided the amount of the refund does not exceed certain limits.<sup>111</sup> The criteria to become an Accredited Officer include competency in auditing and GST matters, particularly refund verification, as well as experience in case management and associated communication.<sup>112</sup>

4.11. If the discretion to retain the refund is exercised, the ATO must inform the taxpayer by no later than 14 days after the lodgment of their BAS (or 30 days in some cases).<sup>113</sup> If the taxpayer is not informed, the ATO is required to pay the GST refund to the taxpayer on the 15th day after lodgment of the BAS.<sup>114</sup>

4.12. Where the taxpayer provides insufficient information or there are discrepancies in the information provided, ATO officers may also request additional information.<sup>115</sup> If the ATO officers have identified issues that may be more appropriately handled by specialist teams they may also escalate the case to other compliance areas in the ATO.<sup>116</sup>

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104 ATO, above n 102, pp 9-11.

105 Ibid, p 11.

106 ATO, *Commissioner's discretion to retain a refund*, above n 40.

107 ATO, 'Commissioner's discretion to retain a refund - frequently asked questions', internal ATO document.

108 *Taxation Administration Act 1953* s 8AAZLGA(2).

109 ATO, 'RI Auditor Guide', above n 53, p 159-160.

110 *Taxation Administration Act 1953*, s 8AAZLGA(2); Explanatory Memorandum, House of Representatives, Tax and Superannuation Laws Amendment (2012 Measures No.1) Bill 2012.

111 ATO, 'RI Auditor Guide', above n 53, p 185.

112 ATO, 'BASE Accreditation Guide', internal ATO document, pp 4-5.

113 *Taxation Administration Act 1953* s 8AAZLGA(3)(a).

114 Explanatory Memorandum, House of Representatives, Tax and Superannuation Laws Amendment (2012 Measures No.1) Bill 2012, p 85.

115 ATO, 'RI Auditor Guide', above n 53, p 158; ATO, 'Pre-issue audit - ITX', internal ATO document, p 7.

116 ATO, 'RI Auditor Guide', above n 53, p 163-168.

4.13. Once ATO officers have the necessary information to make a decision, the case moves to the 'Finalise case and consider referral' stage where officers are required to decide whether to release the GST refund claimed in full or revise the BAS to deny the GST refund claimed in full or in part. Where there is a risk of potential identity theft or identity fraud, the matter may be referred to other more specialised areas of the ATO for action.

4.14. If the ATO does not finalise a case within a certain period of time, the taxpayer has a right of objection against the ongoing retention of the refund.<sup>117</sup> The ATO must inform taxpayers of this right within 7 days of the right being triggered.<sup>118</sup> However, taxpayers may object to the ATO's retention even if the ATO does not notify them.<sup>119</sup> The right to object against the ATO's retention is in addition to taxpayers' general rights of objection contained in Part IVC of the TAA 1953.

4.15. Many stakeholders acknowledge the importance of GST refund verification, noting that, in this regard, the ATO's approaches have been generally working well and taxpayers' and tax practitioners' experience in dealing with ATO officers have been largely positive. However, some stakeholders have raised specific concerns about the ATO's engagement with taxpayers and tax practitioners during the verification process and have suggested a number of improvements.

4.16. Broadly, the specific concerns raised include:

- insufficient communication during the refund verification process, including:
  - inconsistent notification to inform taxpayers of the ATO's retention of their GST refunds within 14 days (or 30 days, as the case may be);
  - insufficient explanation for retention of refunds and adjustments to the relevant BAS ; and
- the ATO's information requests are voluminous and unrelated to the verification of refunds .

4.17. Each of the above concerns are considered in more detail in the specific sections that follow.

4.18. It should be noted that concerns have also been raised regarding the ATO's management of the objection process. These concerns mainly related to the more intensive compliance projects, such as the precious metals industry project. Accordingly, these concerns will be considered in Chapter 6.

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<sup>117</sup> *Taxation Administration Act 1953* s 8AAZLGA(6).

<sup>118</sup> *Taxation Administration Act 1953* s 8AAZLGA(7).

<sup>119</sup> Explanatory Memorandum, House of Representatives, Tax and Superannuation Laws Amendment (2012 Measures No.1) Bill 2012.

## COMMUNICATION DURING THE GST REFUND VERIFICATION PROCESS

### Stakeholder concerns

4.19. In complaints received by the IGT, taxpayers have raised concerns that the notification of the retention of GST refunds by the ATO was much later than 14 calendar days or there was no notification at all.

4.20. Taxpayers with access to the Business Portal, a gateway through which they can access a range of ATO services,<sup>120</sup> may check the status of their BASs and any GST refunds that they may have claimed. However, the Business Portal does not indicate whether the GST refund claim is under review. Accordingly, to find out this information, irrespective of whether taxpayers have access to the Business Portal or not, they have to contact the ATO. In certain cases, the officers responding to such enquiries may not have the necessary information to assist taxpayers.

4.21. An ancillary issue raised by some stakeholders is that the ATO does not inform them when their case escalates from being a verification matter to a broader GST audit.

4.22. Some stakeholders have also observed that the ATO does not always sufficiently explain the reasons for retaining refunds or the underlying risks that it is seeking to address. They believe that without such information, it is difficult to understand the scope of the verification activities or fully engage with the ATO to address its concerns.

4.23. Concerns with a lack of explanation have also been raised by stakeholders where the ATO has fully or partially denied refund claims following reviews or audits. By way of example, a complaint made to the IGT involved a taxpayer who could not understand why a GST debt of \$80,000 was created following adjustments to his BASs. The complainant believed that only \$20,000 claimed in the BASs was the subject of dispute.

4.24. In another complaint made to the IGT, the ATO amended 17 BASs resulting in a debt of \$4,300 to the taxpayer. The complainant did not understand why the ATO had made the adjustments, even after seeking advice from a tax agent and investigating the adjustments with the ATO. Consequently, the complainant believed the ATO had improperly amended his BASs.

4.25. Stakeholders considered that the ATO should provide clearer explanations otherwise it may result in taxpayer confusion or perceptions that the ATO has not appropriately considered all relevant information, leading to unnecessary disputes. Furthermore, communicating specific reasons better informs and educates taxpayers and their representatives leading to potentially improved compliance in the future. It should be noted that concerns raised regarding the lack, or adequacy, of ATO explanations does not necessarily indicate that the ATO decisions were incorrect.

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120 ATO, 'Business Portal' (30 June 2017) <<https://www.ato.gov.au/Business/Business-Portal/>>.

## ATO materials

### Notification to inform taxpayers of the retention of their GST refunds

4.26. As noted earlier, where the ATO has decided to retain GST refunds for verification under section 8AAZLGA of the TAA 1953, the taxpayer is notified within 14 days (or 30 days in some instances) following lodgment of the BAS. The ATO uses a number of communication channels, including telephone, text messages, letter or email to notify taxpayers. The ATO's preference is to inform taxpayers via telephone and thereafter officers may follow up in writing. While the legislation does not require written notification, where a taxpayer requests to be notified in writing, the ATO expects its officers to do so.<sup>121</sup>

4.27. In addition to the guidance provided by PSLA 2012/6, the internal FAQs instruct ATO officers that where notification deadlines fall on a weekend or public holiday, notice may be given on the next working day.<sup>122</sup> The internal FAQs also instruct ATO officers to allow sufficient time for postage in cases where telephone contact is unsuccessful.<sup>123</sup> All communication is required to be documented or attached to the relevant Siebel case.<sup>124</sup>

4.28. Figure 5 below is an extract of the ATO's template notification letter. The letter informs taxpayers of the GST refund retention, the period to which the BAS relates, the ATO actions that may follow, how to access further information on the ATO website and the actions the taxpayer may need to consider as well as the ATO's contact details.

**Figure 5: Extract of ATO notification letter**

**Decision to retain refund under section 8AAZLGA of the *Taxation Administration Act 1953***

Dear <Recipient title, Recipient surname OR Sir/ Madam>

We are writing to let you know that any refund owed to you since lodgment of your activity statement for the tax period <<tax period>> has been retained.

Under tax laws, we are authorised to retain a refund until we have verified the information in your activity statement which relates to the amount, until it is no longer reasonable to verify the information, or until the refund amount changes as a result of an assessment or an amended assessment.

During this time we may:

- release your refund<s>
- offset your refund<s> against other debts you owe
- contact you to discuss the amount<s> claimed
- request additional information to verify the amount<s> you claimed, or
- make an assessment or amended assessment.

For frequently asked questions about our discretion to retain a refund, visit our website [ato.gov.au](http://ato.gov.au) and search for 'Retaining refunds for integrity checks - frequently asked questions'.

**What you need to do**

At this stage you do not need to do anything. We anticipate we will either release your refund or contact you within 14 [OR] 30 days.

Source: ATO

121 ATO, Communication with the IGT, 26 June 2017.

122 *Acts Interpretation Act 1901* s 36(2).

123 ATO, 'RI Auditor Guide', above n 53, p 159.

124 Ibid p 160.



4.29. The requirement for the ATO to notify the taxpayer is important as the consequence for failing to do so results in it releasing the refund. Thereafter, the ATO may only undertake a post-issue audit with a risk that incorrectly released refunds may not be recoverable.

4.30. ATO team leaders are expected to use a mix of approaches to ensure refund decisions are appropriately made and taxpayers notified in accordance with the legislative requirement.<sup>125</sup> These approaches include:<sup>126</sup>

- Adding a note, which includes the date when the retention period expires, to the “ultimate holding company” field in the Siebel case to alert the case officer when a retention decision needs to be made. The Team Leader is able to [sort cases based on this file note] to follow up with the case operative on whether a decision has been made.
- Using spreadsheets of case allocations which includes the notification due date.
- Case reviews or regular case call overs.
- Checking allocated pre issue cases when [officers] are on unplanned leave to ensure retention decisions are made within time.
- Checking Automated Work Allocation [an internal ATO system] to ensure stoppers allocated to officers have been finalised.
- Reviewing stored refund reports.
- Reviewing the Active Compliance Dashboard [a single standardised platform for managers to monitor and report on performance] and/or [Online Analytical Processing] cubes.

4.31. In addition to the above, post-finalisation quality assurance reviews are undertaken via the Sero system, which is used across various business lines to provide feedback to officers on a real time basis.<sup>127</sup> A case is randomly identified for each officer in a given month and assessed by a technical leader from a different BASE team.<sup>128</sup>

4.32. Four primary criteria are to be addressed in making the Sero assessment. Amongst them are specific requirements for assessors to consider whether communication of the retention to the taxpayer has occurred within the required timeframe<sup>129</sup> and whether the officer’s consideration of the 10 statutory factors is

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<sup>125</sup> ATO, Communication with the IGT, 11 August 2017.

<sup>126</sup> Ibid.

<sup>127</sup> ATO, ‘Sero is coming to Refund Integrity Assurance (RIA)’, internal ATO document.

<sup>128</sup> ATO, ‘RIA Sero Matrix’, internal ATO document.

<sup>129</sup> Ibid.

attached to the Siebel case.<sup>130</sup> For completeness, a full list of Sero assessment criteria is contained in Appendix 3.

4.33. Once an assessment is completed in Sero, the team leader reviews it and releases it to the relevant officer. Each case is given one of four ratings, namely: 'Exceeded Standard', 'Met Standard', 'Met Standard Development Required' or 'Standard Not Met'. The Sero assessment result is used to identify any gaps in officer capability and to determine the appropriate training and coaching required to address those gaps.<sup>131</sup>

4.34. A monthly report aggregating the Sero assessments is also developed and provided to team leaders and management. The report summarises the assessments and notes the number of cases where the assessment criteria were met.<sup>132</sup> For the six months between 1 July 2016 and 31 December 2016, the ATO reported 77 per cent of the cases assessed were rated either 'Exceeded Standard' or 'Met Standard'. The ATO reported similar results in the following six months.<sup>133</sup>

4.35. Where a case did not meet the required standard, it does not imply that the ATO's retention decision was incorrect. A case may not have met standard if the ATO officer did not undertake appropriate checks to confirm the identity of the taxpayer or the risk identified by the risk models were not mitigated. If the decision was determined to be incorrect during the Sero assessment process, the case is reopened and the incorrect decision rectified.<sup>134</sup>

4.36. Following an ITX BASE Executive decision<sup>135</sup> to put in place call recording in all of its areas with a large number of telephone calls with taxpayers or their authorised representatives, in 2016, the call recording system, Verint, was introduced to BASE teams.<sup>136</sup>

4.37. Call recording is helpful in resolving some disputes, particularly where the taxpayer's recollection of a telephone conversation may be different to that of the relevant ATO officer. It also allows officers to replay discussions and ensure all relevant details of the conversation are included in contemporaneous notes which are required to be recorded on the Siebel system.<sup>137</sup> ATO officers are expected to appropriately document all their interactions with taxpayers (whether by telephone or otherwise), on the Siebel system and to ensure that their case notes provide sufficient detail.<sup>138</sup>

4.38. During the course of this review, the BASE management team acknowledged that ATO officers' notes in the Siebel system could be improved and have moved to

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130 ATO, 'The 10 factors worksheet', internal ATO document.

131 ATO, Communication to the IGT, 10 October 2017.

132 ATO, 'Indirect Tax BASE Sero Monthly Report: September 2017', internal ATO document.

133 ATO, 'Sero Assessment Overview July to December 2016', internal ATO document; ATO, 'Sero Assessment Overview January to June 2017', internal ATO document.

134 ATO, Communication with the IGT, 19 January 2018.

135 The decision was made in line with recommendations from the ATO's Telephony Reference Group (TRG). The TRG had regard to the ANAO's report into the ATO's *Administration of Contact Centres* (2014).

136 ATO, Communication with the IGT, 20 October 2017.

137 ATO, 'Frequently Asked Questions - ITX BAS Engagement IVR Project', internal ATO document.

138 ATO, Communication to the IGT, 10 October 2017.



introduce training to address this issue. Such training provides specific direction on the importance of quality recording, the use of plain English, the information to be included and the actions or events to be added.<sup>139</sup>

### **Communicating reasons for retention of GST refunds**

4.39. The ATO has committed to improve the client experience, with a strong emphasis on direct officer engagement with taxpayers or their representatives. In line with this commitment, officers are generally expected to communicate their decisions to retain the GST refunds via telephone. They are also required to provide reasons for the decision in terms of the risk identified but not in terms of the 10 statutory factors set out in sub-section 8AAZLGA(2) of the TAA 1953 which they are required to consider.<sup>140</sup> There is no scripting available to them for conducting such telephone calls although guidance is available as to the principles and information that should be conveyed to the taxpayer.

### **Communicating reasons for adjustments to BAS**

4.40. The ATO's RI Auditor Guide requires its officers to record decisions to disallow or vary any GST refund claims on the Siebel system.<sup>141</sup> The decision should contain the following sections:

- What is the compliance issue?
- What are the taxpayer's views?
- What are the facts?
- Supporting evidence
- ATO view
- Decision.<sup>142</sup>

4.41. The RI Auditor Guide also provides further guidance on what information needs to be obtained and included within each of the sections listed above.

4.42. The ATO's internal service standard requires officers to notify taxpayers within seven days of the review or audit decision being made.<sup>143</sup> As part of the ATO's procedure, officers are required to prepare a finalisation letter to inform the taxpayer of the decision in each case except where no further action is required.<sup>144</sup> A range of template finalisation letters has been developed to assist ATO officers in this regard.

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139 ATO, 'Quality notes for compliance BASE presentation', internal ATO document.

140 ATO, Communication with the IGT, 26 June 2017.

141 ATO, 'RI Auditor Guide', above n 53, p 178.

142 Ibid p 174.

143 Ibid p 190.

144 Ibid.

Where the ATO has decided to make adjustments to the taxpayer's BAS, the finalisation letter contains the following information:

- the period of BAS subject to the audit;
- reasons for decision which include relevant facts, issues examined and the explanation for the decision;
- whether a penalty has been imposed;
- how to request remission of general interest charge;
- a fact sheet for paying any tax liability;
- internal review that may be available; and
- objection rights to dispute the assessment.<sup>145</sup>

4.43. In addition to issuing finalisation letters to taxpayers, ATO officers are also required to attempt telephoning taxpayers to inform them of the decision.<sup>146</sup> The information that officers should discuss with taxpayers during such calls is set out in the RI Auditor Guide as well as another internal guide known as the Pre-issue Audit – ITX Procedure.<sup>147</sup>

4.44. In audit cases where a shortfall penalty is not imposed and the total adjustment for all BASs is less than \$5,000, the finalisation of these cases is streamlined.<sup>148</sup> In particular, it is not mandatory to issue a finalisation letter unless the taxpayer has requested it. However, in all cases taxpayers will receive a Notice of Assessment or Notice of Amended Assessment showing the adjustments made by the ATO to their BAS.<sup>149</sup> Further, if the ATO officer finalising the case is an 'Accredited Officer', the decision does not need to be escalated for approval.<sup>150</sup>

## IGT observations

4.45. Many taxpayers are reliant on the prompt payment of GST refunds. Any delay in receiving GST refunds may impact on their cash flow and ability to meet other payment obligations. Therefore, it is important that the ATO maintains efficient verification process, including appropriate procedures and guidance to relevant officers, to expeditiously action refund claims.

4.46. While undertaking this review, the ATO provided a significant range of procedures and instructions that are available to its officers involved in the GST refund verification process. Having examined these materials, the IGT has found that they provide very detailed information regarding most steps in the process. However, they

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<sup>145</sup> ATO, Communication with the IGT, 11 August 2017.

<sup>146</sup> ATO, 'RI Auditor Guide', above n 53, p 190.

<sup>147</sup> Ibid pp 190-191.

<sup>148</sup> Ibid p 169.

<sup>149</sup> Ibid.

<sup>150</sup> Ibid.

are voluminous and not well structured and may overwhelm ATO officers, particularly those that may be new to the task.

4.47. By way of example, the RI Auditor Guide contains more than 200 pages when printed. There are also numerous links that further sub-link to other procedures or guidance. The net result is that there is overlap and redundancy in the procedures, with critical instructions being lost or difficult to locate amongst a range of internal administrative requirements. This is demonstrated by some procedures requiring taxpayers to be contacted by the 'required date' without stating how to determine that date. The RI Auditor Guide itself refers to the notification requirements in three separate sections.

4.48. In addition to the RI Auditor Guide, the Pre-issue Audit – ITX Procedure instructs officers that, 'you must inform the taxpayer by the required date (the 14<sup>th</sup> day after lodgment) if you are retaining the refund'. The internal FAQs also contain information on the notification requirements. These procedures are variously cross-referenced to each other sending officers in both directions for more information.

4.49. The IGT considers that the ATO's procedures need to be consolidated and streamlined to remove duplication, improve officers' understanding and access to relevant information, thereby achieving administrative efficiency.

4.50. In the course of the IGT review, the ATO advised that it had commenced reviewing the RI Auditor Guide with a view to streamlining the document. A consultation group consisting of a range of officers at various levels was formed to better understand case officers' experiences in using the procedures.<sup>151</sup> The first stage of the review is to separate the guide into five main areas:

- BAS Engagement standalone procedures
- Job Aids
- Checklists
- Administration
- Learning and Development material.<sup>152</sup>

4.51. The second stage is to review the information to ensure it is fit for purpose, develop new procedures for each of the above five areas and host it on Sharepoint, an online internal web page accessible to all officers.<sup>153</sup>

4.52. The ATO has not indicated when it expects to finalise the review and complete the updating of the RI Auditor Guide.

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<sup>151</sup> ATO, Communication with the IGT, 20 October 2017.

<sup>152</sup> ATO, Communication with the IGT, 20 October 2017.

<sup>153</sup> ATO, Communication with the IGT, 20 October 2017.

## **Notification informing taxpayers of GST refund retention**

4.53. The current ATO process to monitor and comply with the legislative notification requirement is done manually and as a consequence is reliant upon ATO officers correctly calculating and recording notification deadlines. Moreover, ATO officers are required to record notifications by attaching the relevant email, letter or file note of the telephone conversation on the Siebel system. The IGT's sample testing of the ATO's file notes suggests that sufficient information was provided to taxpayers in most instances and taxpayers were informed of the refund retention.

4.54. The Verint system provides certain assurances by recording all telephone interactions. However, despite the availability of the Verint system, ATO officers are required to ensure that their Siebel notes are a detailed and accurate reflection of their interaction with taxpayers. The IGT considers that the ATO should ensure all ATO officers' file notes are robust such that compliance with key legal requirements is evidenced and readily available to address any taxpayer challenge or dispute.

4.55. In monitoring compliance of the notification requirement, team leaders currently rely on manual processes which increase the risk of deadlines being missed or not identified early enough for remedial action to be taken. In addition, there are no procedures or guidance on how a team leader manages the notification requirement or how assurance is evidenced. This will likely lead to varying and inconsistent practices across different BASE teams within the ATO.

4.56. While the Sero assessment process does consider whether taxpayers are notified of the retention within 14 days, not all cases are subject to this assessment and, in any event, it is only undertaken after the case has been finalised. The IGT notes that the ATO does not undertake any other internal quality assurance audits to determine the proportion of all cases which do and do not comply with the notification requirements.

4.57. Given that the notification requirement is a legislative one, the ATO needs to be assured that it is met in all cases. Accordingly, the IGT believes that, to the extent possible, there should be automatic triggers that alert officers or team leaders of the notification deadline where it has not been met already. For example, this could be achieved through the use of automated flags or indicators on the Siebel system. Such improvements would be particularly useful to team leaders where relevant officers take unscheduled leave, resign, or experience high workloads.

4.58. Towards the latter stages of this review, the IGT was advised that a new function in the RAPT system was currently being developed which may partially address the above issue. The new function is intended to provide ATO officers with the following relevant BAS information:

- Tax period of the BAS lodged
- Lodgment source
- Lodgment date
- Label 9 net amount (payment or refund amount of the BAS)

- Number of days since lodgment
- Date of the end of the 14 day period to notify taxpayers of the retention
- Date when 60-day call over is due
- Date when objection rights are triggered (not including any extensions to the 60-day period as a result of ATO's information request).<sup>154</sup>

4.59. It should be noted that the above is not in the form of an alert as envisaged by the IGT. Furthermore, it is developed within RAPT rather than Siebel. The IGT believes it would be preferable that officers be alerted in the Siebel system as cases are actioned through it. It is also important that all information is recorded and available on a single system, that is, Siebel, rather than through multiple sources to avoid officer confusion and support more efficient administration.

4.60. The IGT acknowledges that the legislative timeframe of 14 days may at times pose operational challenges for the ATO, in particular, when taxpayers lodge their BAS in paper form or where the ATO has detected potential fraud or serious non-compliance. It may not provide sufficient time for ATO officers to fully consider all information and risks before making the decision to retain the GST refunds. As a result, they may err on the side of caution and retain a refund which may have otherwise been released and thereby unnecessarily disadvantage affected taxpayers.

4.61. Whilst the above are valid concerns, the IGT considers that the implementation of the recommendations in this report will improve the efficiency of the verification process and that the 14 day notification period may be sufficient. Accordingly, it would be appropriate to allow some time for the outcome of this review to bear fruit before reconsidering the length of the notification period. However, a different approach may be required in cases of serious non-compliance or potential fraud and this is explored in Chapter 6.

### **Communicating and documenting reasons for retention of GST refunds**

4.62. Whilst there is no legislative requirement for the ATO to provide reasons for retaining refunds, it is good administrative practice to do so. It avoids disputes and fosters confidence in the revenue agency and the system as a whole – a key factor in promoting voluntary compliance. The ATO does seek to provide reasons to some extent but its associated documentation could be improved.

4.63. As mentioned earlier, ATO officers are generally expected to communicate their decisions to retain GST refunds via telephone as well as the reason for such a decision in terms of the risk identified but not in terms of the 10 statutory factors. Given there is no scripting available to them for such calls, it is important that they accurately record those discussions in a file note so that team leaders can assess the taxpayer experience as well as the officers' performance without resorting to listening to hours of call recordings.

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<sup>154</sup> ATO, Communication with the IGT, 20 October 2017.

4.64. Figure 5, which reproduces the template used to inform taxpayers in writing where telephone contact has not been possible, provides no reason for the decision at all. This is inconsistent with the guidance for conducting the same task via telephone. This template also refers taxpayers to the ATO website for further information. Specifically, taxpayers are advised to search for the term 'Retaining refunds for integrity checks – frequently asked questions'. However, the IGT's testing of that search term, or its subsets, did not yield any relevant results.

4.65. Whilst officers are not required to discuss their decision with taxpayers in terms of the 10 statutory factors, they are required to document their consideration of these factors. The method of such documentation varies between different ATO teams. It may be in Excel spreadsheets, Word templates or Siebel notes. The Word template includes 'tick boxes' and officers may input additional comments, the Excel spreadsheet includes non-mandatory free text dialogue boxes for input and Siebel notes are purely free text. As a result, the quality and level of detail in these documents can vary significantly amongst the various teams. The IGT has reviewed such documents in a random sample of 40 cases.

4.66. From the IGT's review of the above sample, it was not apparent how officers had considered each of the 10 factors. In three cases, there was no documentation in this regard. In the majority of the other cases, there was insufficient or inadequate consideration of the factors either individually or as against each other. In some cases, a 'tick box' approach was used to simply confirm that an action was recorded in the Siebel system without referencing the location on Siebel or what was actually recorded. More concerning is that in some instances, a box had been ticked confirming that no discussion with the taxpayer has taken place whilst in others no boxes had been ticked at all.

4.67. Accordingly, significant improvement is necessary in how ATO officers document their consideration of the 10 statutory factors and there needs to be consistency in the manner it is done across the various teams. Such lack of documentation suggests that the factors may not be appropriately considered or at the very least does not allow the team leaders to assess officers' performance and their decisions.

### **Communicating reasons for adjustments to BAS**

4.68. Taxpayers have a right to understand the reasons for any ATO action, including an adjustment of their BAS. In high volume, low value, less complex cases, the ATO is likely to be dealing with taxpayers who do not often engage with the tax system. In such cases, the ATO communication with the taxpayer should be in plain English and tailored to their circumstances to ensure they fully understand the relevant issues.

4.69. As mentioned earlier, whilst the ATO provides some guidance on how to conduct telephone calls for explaining adjustments, there is no scripting available for such calls. Accordingly, officers' file note of these calls should be fulsome and accurately reflect the conversation, particularly where there is no follow-up written confirmation to taxpayers. The IGT has reviewed a sample of such files notes.



4.70. From the IGT's review of a sample of the file notes, a number of them were written in disjointed short form or contained ATO jargon. When these file notes were read in isolation, they did not contain sufficient information for a third party to understand the reasons for the adjustments. It is not apparent whether these file notes accurately reflect the conversation that had taken place between the taxpayer and the ATO officer.

4.71. Consistent with the earlier IGT observations regarding notification requirements, improving the quality and accuracy of file notes in these circumstances is also important to evaluate the taxpayer experience as well as the performance of the relevant officers.

#### **RECOMMENDATION 4.1**

*The IGT recommends that, in respect of pre-issue GST refund verification, the ATO:*

- (a) *consolidate and streamline its guidance to its officers with an emphasis on adhering to the statutory requirements;*
- (b) *ensure that interactions between its officers and taxpayers as well as its officers' consideration of statutory requirements are accurately and consistently documented and that team leaders use such documentation to assess the performance of officers and the taxpayer experience;*
- (c) *provide a mechanism to automatically alert its officers and team leaders to notify taxpayers of the retention of their refunds within the statutory period; and*
- (d) *improve its communication with taxpayers by ensuring that they are provided with sufficient reasons for the retention of their refunds and the other information provided to them is accurate and up to date.*

#### **ATO RESPONSE**

##### **(a) Agree**

The report acknowledged that work was already underway to streamline our processes and procedures. This was progressed during the course of this review and has now been finalised. The ATO is committed to continuous review and improvement of our guidance for staff.

##### **(b) Agree**

The ATO provide clear guidance for its staff on the statutory requirements through guidance in *PSLA 20012/6 Exercise of Commissioner's discretion to retain a refund* and in internal Frequently Ask Questions document. The Indirect Tax BAS Engagement (BASE) branch, which undertakes the vast majority of verification activities on GST refunds, is currently reviewing its documentation of the 10 statutory factors in making decisions to retain a refund.

##### **(c) Disagree**

Activity statements are processed through the Instalment Processing System (IPS). This system does not allow for automatic alerts to notify officers or Team Leaders whether retention of a refund has been made within the statutory period in s8AAZLGA of the *Taxation Administration Act 1953* (TAA 1953).

The ATO is planning to move the processing of activity statements to the Integrated Core Processing (ICP) system, which may provide opportunities to build alerts. In the meantime the ATO has a number of reporting options that can be used to ensure staff are making appropriate decisions with the statutory requirements.

**(d) Agree**

We are currently reviewing all correspondence to ensure that communication with taxpayers is clear and easily understood. The 'retention of refund' letter used in BASE will provide reasons why a refund is being held for further verification.

## **ATO INFORMATION REQUESTS**

### **Stakeholder concerns**

4.72. In complaints and submissions to the IGT, concerns have been expressed about the ATO's wide ranging information requests, which are not tailored to taxpayers' circumstances, without any explanation as to how they relate to the risk that the ATO has identified. At times, the information requested may already be readily available to the ATO, for example from prior reviews.

4.73. Stakeholders believe that information requests may go beyond ascertaining that the GST refund claim made in a BAS is correct. By way of example, the ATO may request information about the taxpayer's business such as their marketing strategies or suppliers. These stakeholders believe that to verify the validity of refund claims, the information request should be limited to such material as invoices and bank statements.

4.74. A number of stakeholders have also suggested that more experienced practitioners can forecast situations where the ATO is likely to retain a GST refund based on the specific risk or quantum of the refund. In these circumstances they pre-empt the refund retention by preparing materials in advance and then forwarding these contemporaneously with the BAS lodgment to assist the ATO verification process and expedite the refund release. These stakeholders believe that taxpayers should be able to upload such information onto the ATO system at the same time as lodging their BAS.

### **ATO Materials**

4.75. The ATO requests information from taxpayers as part of its verification activities. Sub-section 8AAZLGA(4) of the TAA 1953 states that:

*In informing the entity that the amount is retained, the Commissioner may request information that he or she is aware will be required for the purposes of verifying the notified information.*



4.76. The ATO's preference for seeking information from taxpayers is to do so informally and by telephone, where possible.<sup>155</sup> In preparation for telephone contact, the RI Auditor Guide provides some questions, by way of example, that ATO officers may ask taxpayers or their representatives.<sup>156</sup> The questions are intended to gain a better understanding of the taxpayer's business to determine whether the taxpayer is carrying on an 'enterprise' and determine the reason for the refund claim.<sup>157</sup>

4.77. If telephone contact is unsuccessful or the taxpayer requests that the questions be provided in writing, general business profile questionnaires have been developed to provide guidance to officers on relevant questions.<sup>158</sup> The ATO also has industry specific questionnaires which were developed following consultation with industry representatives.<sup>159</sup> The ATO has not advised the IGT how often these industry specific questionnaires are reviewed or how it receives feedback on them.

4.78. The ATO also has a standard letter for requesting information and officers may tailor the information request based on taxpayers' circumstances.<sup>160</sup>

4.79. On receiving the requested information from taxpayers or their representatives, ATO officers are instructed to consider whether the identified risk(s) may be mitigated without further materials. If further information is required to mitigate the risk, the RI Auditor Guide provides a list of suggested further information:

- bank statements for the period until audit (irrespective of cash or non-cash basis of accounting);
- a list of all transactions for the period;
- tax invoices for the period (the number required to be determined by you during your interview);
- proof of finance;
- for importers – Import Declaration form (N10) and Official Receipt; and
- for exporters – Export Declaration Number (EDN) and Bills of lading.<sup>161</sup>

4.80. In seeking such further information, ATO officers are also instructed to negotiate a timeframe that is reasonable for both the taxpayer and the ATO. In doing so officers must have regard to the notification requirements under section 8AAZLGA of the TAA 1953 and the time needed to assess the risk and make a decision regarding the refund retention.<sup>162</sup> Generally up to a maximum of 14 days is considered appropriate

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155 ATO, *Our Approach to Information Gathering* (26 July 2016) <<https://www.ato.gov.au/>>.

156 ATO, 'RI Auditor Guide', above n 53, p 119.

157 ATO, 'RI Auditor Guide', above n 53, p 121.

158 Ibid.

159 Ibid p 119.

160 ATO, Communication with the IGT, 11 August 2017.

161 ATO, 'RI Auditor Guide', above n 53, 119.

162 Ibid, p 136.

for the provision of the information.<sup>163</sup> If the ATO makes a second request for the information, the ATO generally provides an additional 14 days.<sup>164</sup>

4.81. If a taxpayer has not provided all requested documents or further clarification is required, the ATO may issue additional information requests.<sup>165</sup> Taxpayers are also provided with opportunities to explain any discrepancies identified by officers.<sup>166</sup>

## IGT Observations

4.82. The IGT notes that ATO procedures require officers to conduct extensive profiling before contacting taxpayers to request further information in support of GST refund claims. The profiling process, if completed correctly, should ensure all information available to the ATO has been verified prior to taxpayer contact and thereby reduce the scope of the information requested.

4.83. A close examination of the ATO's information request templates and associated procedures supports taxpayers' perception that some of the information requests are unreasonably extensive and not directly relevant. Examples of questions in the template include: 'How do you advertise your business?' and 'How are you funding the enterprise?'. It is important for the ATO to explain that this information is required for the ATO to establish whether the taxpayer is carrying on an enterprise.

4.84. Furthermore, the use of general questionnaires, as opposed to industry specific ones, is unlikely to result in a tailored and considered approach to seeking information. In working to ensure that such questionnaires remain relevant to taxpayers and the risks to be addressed, the ATO should periodically consult with internal and external industry experts to refine and update the questionnaires.

4.85. Even if industry specific questionnaires were used, some profiling questions may be viewed by taxpayers as being irrelevant to refund verification. In such cases, it is important that ATO officers explain the reasons for asking such questions and how it addresses the risks identified by the ATO's risk assessment tools. The ATO's general guidance on information gathering contemplates only limited situations in which the ATO would not explain its reasons for seeking information, including where it may prejudice ongoing investigations or breach secrecy or privacy provisions.<sup>167</sup>

4.86. There is limited guidance to officers regarding communication of reasons for information requests. Provision of such reasons or explanation improves their confidence in the system and enhances voluntary compliance as well as assisting them in pinpointing the required information.

4.87. There is also minimal written guidance available to officers in relation to the period of time in which taxpayers must respond to information requests where the

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163 ATO, RI Auditor Guide, above n 53, p 134; ATO, Communication with the IGT, 14 December 2017.

164 ATO, Communication with the IGT, 14 December 2017.

165 ATO, RI Auditor Guide, above n 53, p 148.

166 Ibid, p 158.

167 ATO, above n 155.

request is made in writing only. Such limited guidance may lead to inconsistencies in the timeframes given to taxpayers across BASE teams.

4.88. In relation to a formal process for pre-emptively providing supplementary information to the ATO, in anticipation of a retention of refunds, the IGT considers that, whilst it may be useful in some cases, it may place an unnecessary additional burden on taxpayers in other instances. However, it is important to note certain tax practitioners and taxpayers, who have sufficient networks and direct contact with ATO officers, are able to take such pre-emptive action on an informal basis. This may give rise to perceptions of lack of transparency and inconsistent treatment.

#### **RECOMMENDATION 4.2**

*The IGT recommends that, in undertaking pre-issue GST refund verification, the ATO:*

- (a) *periodically review its information requests templates with input from stakeholders, including industry experts, to ensure that those requests are appropriately focused on addressing the risks identified; and*
- (b) *consider allowing taxpayers and tax practitioners to pre-emptively provide information online to assist in the timeliness of the verification process.*

#### **ATO RESPONSE**

##### **(a) Agree**

We are committed to ensuring information requests are tailored according to the risk identified through our risk assessment tools and client profiling. We will also review our profile questionnaires using industry experts to ensure the questions are appropriately focused.

##### **(b) Disagree**

Taxpayers and Tax Agents who lodge electronically already have the option to supply supporting information through the various portals. The ATO believes that the current options are appropriate considering the very small number of refund activity statements stopped for verification activities. Allowing taxpayers to send in information may result in additional compliance costs where their refund is not subject to verification activities.

## **AUDIT AND OBJECTION TIMEFRAMES**

### **Stakeholder concerns**

4.89. While stakeholders have generally acknowledged that the GST refunds process works well, concerns have been raised about the timeliness of the ATO's verification activities. They have indicated that audit timeframes may be prolonged as a result of insufficient communication between the ATO and taxpayers or where the ATO requests extensive information from taxpayers.

4.90. The ATO's information requests may also delay taxpayers' objection rights which are generally triggered if the ATO has not finalised the audit within 60 days. However, where the ATO has issued a request for information, the elapsed audit timeframe is paused ('stop the clock') until the requested information is provided.

4.91. As the calculation of time elapsed can be complicated due to 'stop the clock', taxpayers rely on the ATO informing them when their rights have triggered. Some stakeholders and complainants, who have approached the IGT, have noted that ATO does not always inform them of their objection rights being triggered within the legislated timeframe.

4.92. Furthermore, where objections have been lodged, the time taken by the ATO to consider and issue decisions far exceeds the ATO's previous service standard of 56 days. In certain cases made known to the IGT, taxpayers had to exercise their rights to compel the Commissioner to make a decision.<sup>168</sup> These concerns seem to arise in audits involving the precious metals industry, which is discussed in Chapter 6 of this report, rather than in BAU cases. However, it is nonetheless instructive to examine the timeliness of the ATO's verification activities and the ATO's notification of objection rights in the BAU context.

## ATO materials

### Time taken by the ATO to verify GST refunds

4.93. Section 8AAZLGA of the TAA 1953 does not specify a definite period for which the ATO must finalise its verification and release the refund. However, it states that:

- (1) *The Commissioner may retain the amount under this section only until:*
  - (a) *if paragraph (1)(a) applies--it would no longer be reasonable to require verification of the information; or*
  - (b) *if the Commissioner fails to inform the entity, in accordance with subsection (3), that he or she has retained the amount under this section--the end of the day after the time by which, under that subsection, the Commissioner is required to inform the entity; or*
  - (c) *in any case--there is a change to how much the Commissioner is required to refund, as a result of:*
    - (i) *the Commissioner amending an assessment relating to the amount; or*
    - (ii) *the Commissioner making or amending an assessment, under Division 105 in Schedule 1, relating to the amount;*

*whichever happens first.*<sup>169</sup>

4.94. PSLA 2012/6 and internal FAQs reiterate the legislative provision above<sup>170</sup> and reinforce the need for ATO officers to 'review each retention decision from time to

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<sup>168</sup> Taxation Administration Act 1953 s 14ZYA.

<sup>169</sup> Taxation Administration Act 1953 s 8AAZLGA(5).

<sup>170</sup> ATO, *Commissioner's discretion to retain a refund*, above n 40; ATO, above n 107, p 11.

time by reference to the particular circumstances<sup>171</sup> of the taxpayer and whether it is still reasonable for the ATO to retain the refund.

4.95. The timeframes taken for the ATO to undertake its verification activities in BAU audit cases are set out below in Tables 4 and 5. They show that in 2014-15, 2015-16 and 2016-17 financial years, over 50 per cent of cases were finalised within 14 days.<sup>172</sup>

**Table 4: Overall case finalisation in percentages**

Number of days	Year ending 30 June					
	2015		2016		2017	
	Reviews	Audits	Reviews	Audits	Reviews	Audits
0-14 days	53.06%	13.30%	45.89%	11.50%	39.72%	10.59%
15-28 days	13.03%	4.55%	15.34%	5.24%	18.76%	5.37%
29-60 days	5.54%	5.37%	8.82%	6.73%	12.32%	7.50%
61-90 days	0.54%	2.47%	0.79%	2.88%	0.53%	3.14%
>90 days	0.10%	2.05%	0.18%	2.63%	0.20%	1.90%
<b>Total number of cases</b>	<b>33,350</b>		<b>27,455</b>		<b>23,313</b>	

Source: IGT - Constructed from ATO source information.

**Table 5: Overall case finalisation in numbers**

Number of days	Year ending 30 June					
	2015		2016		2017	
	Reviews	Audits	Reviews	Audits	Reviews	Audits
0-14 days	17,695	4,434	12,600	3,157	9,259	2,468
15-28 days	4,344	1,516	4,211	1,438	4,373	1,251
29-60 days	1,848	1,791	2,421	1,849	2,871	1,748
61-90 days	181	823	218	790	123	732
>90 days	33	685	50	721	46	442
<b>Total number of cases</b>	<b>33,350</b>		<b>27,455</b>		<b>23,313</b>	

Source: IGT - Constructed from ATO source information.

4.96. Table 6 shows the average time taken to finalise cases for the years 2014-15, 2015-16 and 2016-17 as recorded in the Siebel system.

**Table 6: Average days taken for the ATO to finalise its verification**

	Year ending 30 June					
	2015		2016		2017	
	Reviews	Audits	Reviews	Audits	Reviews	Audits
Mean	13	32	15	36	17	35
Median	10	16	11	21	13	23

Source: IGT - Constructed from ATO source information.

4.97. On the whole, the statistics show that the vast majority of cases are finalised within 60 days. Across all three financial years, the majority of cases were completed within 14 days (66.36 per cent in 2014-15, 57.39 per cent per cent in 2015-16 and 50.31 per cent in 2016-17) although there has been a reduction in the number of cases finalised within 14 days in 2016-17 compared to 2014-15 and 2015-16. The ATO has

171 ATO, *Commissioner's discretion to retain a refund*, above n 40, paras 9 and 13.

172 ATO, 'Case Outcomes by Age', above n 50.

attributed this reduction to the increase in case complexity.<sup>173</sup> The proportion of cases retained beyond 60 days has consistently been less than 7 per cent (5.16 per cent in 2014-15, 6.48 per cent in 2015-16 and 5.77 per cent in 2016-17).

4.98. The ATO has reported that in 2016-17, 94.1 per cent of its audit and review cases were finalised within cycle time, exceeding its 80 per cent service standard.<sup>174</sup>

### Notification of objection rights being triggered

4.99. A key legislative addition, following the enactment of section 8AAZLGA of the TAA 1953, was the inclusion of specific objection rights against ongoing retention of refunds by the ATO, which arise 60 days after refunds have been retained.<sup>175</sup>

4.100. The 60 day period may be extended where taxpayers are required to respond to ATO information requests.<sup>176</sup> The ATO's procedures instruct its officers to consider the effects that information requests may have on taxpayers' objection rights. Specifically it states that ATO officers need to:

*Consider the effects that waiting periods for any additional information requests will have on taxpayers review rights of the retention decision under 8AAZLGA.*

4.101. The ATO must inform taxpayers within 7 days of the objection rights being triggered. Specifically, sub-section 8AAZLGA(7) of the TAA 1953 states:

*Before the end of the 7 days after the start of the period during which, under section 14ZW, the entity may object to the decision, the Commissioner must notify the entity, in writing, that the entity may object to the decision.*

4.102. The Explanatory Memorandum provides the following example to illustrate the relevant timeline: a taxpayer lodged its BAS for the tax period ending 30 June 2012 on 28 July 2012 claiming a GST refund. After considering the 10 statutory factors, the ATO decided that verification was required. On 8 August 2012, the ATO informed the taxpayer of their decision to retain the refund under section 8AAZLGA of the TAA 1953. On 20 August 2012, the ATO requested additional information from the taxpayer which was provided on 19 September 2012. Note the effect is such that the 60 day timeframe is effectively extended by the time the taxpayer takes to respond. If by 10 October 2012, the ATO still had not refunded the amount or made an assessment, the taxpayer may object to the ATO's decision to retain the amount under Part IVC of the TAA 1953. The ATO is required to notify the taxpayer of their objection rights by 17 October 2012.<sup>177</sup>

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173 ATO, Communication with the IGT, 20 October 2017.

174 ATO, Communication with the IGT, 20 October 2017.

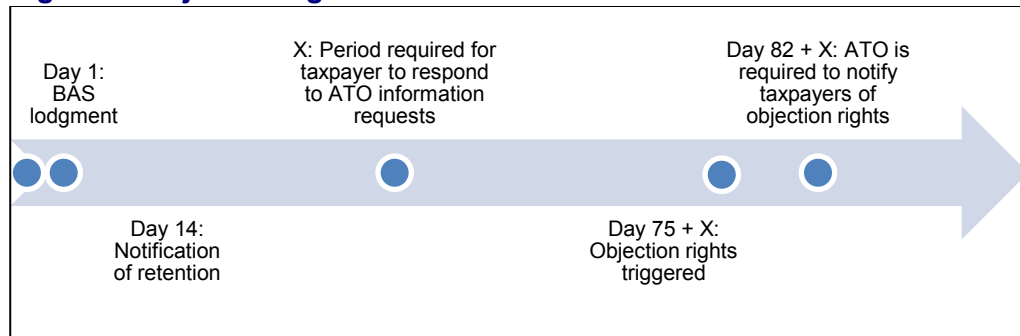
175 *Taxation Administration Act 1953 s 14ZW(1)(aad)*.

176 *Taxation Administration Act 1953 s 14ZW(4)*.

177 Explanatory Memorandum, House of Representatives, Tax and Superannuation Laws Amendment (2012 Measures No.1) Bill 2012, p 85.

4.103. An illustration of the timeline leading to the objection rights being available is produced in Figure 6.

**Figure 6: Objection rights timeline**



Source: IGT

4.104. The ATO's internal FAQs provide guidance to officers on when the ATO is required to inform the taxpayer of their objection rights against ATO retention. Specifically it states that:

*The Commissioner is required to inform the entity in writing about the right to object against the decision to retain a refund. The Commissioner must inform the entity before the end of 7 days after the end of the 60-day period (or as extended).<sup>178</sup>*

4.105. The ATO has advised the IGT that an automated tool within the BAS Analyser, called the Retention of Refund Analyser (RoRA) is available for its officers to calculate time elapsed on a retention case, including any 'stop the clock' periods as a result of information requests. The tool requires the officer to manually input the relevant dates of when the information was requested and received. The RoRA tool then calculates the date that the objection rights are triggered.

4.106. Once the objection right has triggered, the ATO's guidelines instructs its officers to prepare and send correspondence to taxpayers informing them of their objection rights.<sup>179</sup> The ATO has developed template correspondence to assist its officers in this regard. Figure 7 below is an extract of such correspondence.

<sup>178</sup> ATO, Frequently Asked Questions – ITX, above n 137.

<sup>179</sup> ATO, 'Guidelines for retention of refunds under section 8AAZLGA of the TAA 1953 in pre-issue cases', internal ATO document.



**Figure 7: Letter notifying taxpayers of their objection rights**

**Your right to object to the decision to retain your refund**

Dear <Recipient title, Recipient surname OR Sir/Madam>

We are writing to advise you that your activity statement refund for the tax period <<tax period>> has still been retained and you now have the right to object to this decision. This is because we have retained your refund for more than 75 days. *[or]* we have retained your refund for more than 75 days, plus the time you took to supply the information we requested.

We have decided to retain your refund for the following reasons:

- <insert reasons>
- <repeating dot point for each reason>.

**How to object**

If you decide to lodge an objection, it needs to:

- be in writing
- be signed and dated, and
- detail the grounds you are relying on.

Your objection must be lodged prior to the release of your refund or the Commissioner making or amending your assessment. Once one of these has occurred you are unable to object to our decision to retain your refund. .

You can, however, object to the assessment or amended assessment.

Source: ATO

4.107. It should be noted that taxpayers may lodge an objection against the ATO's retention even if the ATO fails to notify them of their objection rights.<sup>180</sup> The ATO's RI Auditor Guide informs officers that 'where a refund has been retained for verification, objection rights to the decision arise at 60 days (plus any applicable extensions)'.<sup>181</sup>

4.108. ATO's statistics show that the utilisation of objection in BAU cases is low, with only 3 objections received since 1 July 2015. Of those, two were disallowed whilst the third became invalid as a result of the refund issuing prior to the objection decision being made.

## IGT observations

4.109. It is clear from the discussion above that the majority of BAU cases are completed well before objection rights are triggered (that is, within 75 days). Completion within this time period should be encouraged for the efficient operation of the system as well as minimising unnecessary costs associated with objection and litigation. However, even in those cases where objection rights have been triggered, the uptake by taxpayers has been low which may be due to a range of reasons.

<sup>180</sup> *Taxation Administration Act 1953*, s 8AAZLGA(8); ATO, *Commissioner's discretion to retain a refund*, above n 40, para 16.

<sup>181</sup> ATO, 'RI Auditor Guide', above n 53, p 182.



4.110. Firstly, taxpayers may not be aware that their objection rights have been triggered due to the complexities associated with calculating the days elapsed including any extensions due to further information requests being made by the ATO. Using case data provided by the ATO, the IGT sought to examine the ATO's compliance with the requirement to notify taxpayers of their objection rights. That exercise proved difficult due to a number of factors including:

- the absence of a clear indicator in the Siebel system as to whether objection rights had been triggered;
- the multiple dates relevant to the particular case such as BAS lodgment, case creation and case allocation; and
- the absence of a clear indicator of time elapsed throughout the case and any extensions as a result of additional information requests.

4.111. While the BASE teams have access to the RoRA tool which they may use to track the 60-day objection period and any extensions resulting from information requests, the IGT understands that it is not mandatory for officers to use it. As taxpayers rely on the ATO to correctly calculate the 60-day period and to inform them when their specific retention objection rights have been triggered, the IGT is of the view that the ATO should make use of the RoRA tool in all cases where it makes information requests.

4.112. Secondly, the time and costs associated with pursuing objections may be considerable. Accordingly, taxpayers may be reluctant to take such a course of action particularly as it would be solely aimed at the retention decision rather than any amendment to the BAS.

4.113. Thirdly, there is a risk that when a taxpayer objects or seeks review of the retention decision, it could be rendered moot by the Commissioner issuing an amended assessment, as illustrated in *Sanctuary Australasia Pty Ltd v Commissioner of Taxation*.<sup>182</sup> In that case, the Administrative Appeals Tribunal (AAT) ruled that the taxpayer had no standing to seek a review of the objection decision as the Commissioner had issued an amended assessment.<sup>183</sup>

4.114. Ultimately, any decisions regarding whether to exercise a right to object to the retention of a refund will be made by the taxpayer in consultation with their representatives. The ATO's responsibility is to ensure that taxpayers are aware of their right to lodge such an objection, notify them as to when the right has been triggered and to provide information that assists them to lodge such objections effectively.

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<sup>182</sup> *Sanctuary Australasia Pty Ltd v Commissioner of Taxation* [2013] AATA 371.

<sup>183</sup> *Sanctuary Australasia Pty Ltd v Commissioner of Taxation* [2013] AATA 371 at [4].

4.115. In submissions to the IGT, it had been suggested that rather than requiring taxpayers to go through an objection process, the taxpayer should have a right to seek an independent external review of the retention decision. Such an approach may benefit both the ATO and the taxpayer. The taxpayer has a degree of certainty in knowing that there is a maximum period of time under which the Commissioner may retain a refund and to plan their resources and operations accordingly. The ATO, on the other hand, would not have to notify taxpayers of their objection rights and deal with resulting objections whilst also conducting audits.

4.116. It should be noted however that an external review mechanism may be just as costly for taxpayers as the current objection process and would only be aimed at the ATO's retention of the refund rather than the substantive amendment to their BAS. Moreover, taxpayers currently have external channels available to them to raise their concerns, including seeking judicial review under the *Administrative Decisions (Judicial Review) Act 1977*. In addition, whilst it would not result in a binding determination, taxpayers may seek the assistance of the IGT through his complaints handling service if they believe that there has been undue delay in the ATO's verification activities.

#### **RECOMMENDATION 4.3**

*The IGT recommends that the ATO:*

- (a) *make effective use of its automated system to calculate the 60-day period within which taxpayers may lodge an objection and inform them accordingly; and*
- (b) *provide information to assist taxpayers in lodging such objections effectively.*

#### **ATO RESPONSE**

##### **(a) Agree**

The ATO currently has automated systems available for staff to calculate when taxpayers' rights to object are triggered taking into account any extensions to the 60 day statutory period associated with information requests. The ATO will reinforce with its operational staff to use the available system in those cases where objection rights are likely to be triggered.

##### **(b) Disagree**

The ATO currently provides information to taxpayers to advise them of their objection rights and how to lodge an objection. This information is clearly communicated in written correspondence when the taxpayer's objection rights are triggered. The ATO also provides information on our website, '*How to object to a decision*'.

The ATO considers the information that is currently made available to taxpayers is sufficient to assist them in lodging an objection.

## MANAGEMENT OF IDENTITY FRAUD

### Stakeholder Concerns

4.117. An allegation has been made to the IGT that the ATO's risk assessment tools do not accurately detect identity fraud and GST refund fraud nor does it differentiate between them. In particular, reference was made to internal ATO operations, active between 2011 and 2012, where it was alleged that crude risk assessment tools incorrectly identified certain cases as involving identity fraud rather than potentially incorrect GST refunds. As a result, the wrong action was taken, including the cancellation of taxpayers' ABNs, denying their refunds without appropriate communication and effectively denying them review and objection rights.

4.118. A related concern identified was that as a result of erroneously classifying certain cases as 'identity fraud', the relevant accounts were 'locked down' and were not subjected to further compliance action for other potential breaches.

### ATO materials

4.119. The ATO has advised the IGT that it had in place a number of operations to address specific risks between 2011 and 2012.

4.120. In 2011, one of the automated risk assessment tools discussed in Chapter 3, identified a group of 200 trusts that had been set up using stolen identities.<sup>184</sup> As a result, the ATO initiated a 'fast actioning' operation, codenamed Whip, given the serious nature of the risks. It involved taking a range of actions including retention of refund and cancellation of ABN or GST registrations. In addition, 47 entities were identified for further verifications or audits.<sup>185</sup> This streamlined approach provided ATO officers with discretion as to whether communication with taxpayers was necessary.<sup>186</sup> Interaction or correspondence in these cases would only occur where the taxpayer successfully proved their identity through the ATO's proof of identity process.<sup>187</sup>

4.121. Operation Whip was similar to other operations that were active at the time, variously codenamed Zodiac, Cohort,<sup>188</sup> Onion and Feline, to address risks that had been identified within specific groups. In each of these operations, communication with taxpayers was either deemed unnecessary or left to the discretion of the ATO officer. Moreover, in the case of Operation Cohort, the internal ATO instructions stated that no notices of assessments or audit finalisation letters would be issued and therefore no objections rights would be available. However, the instruction also noted that there could be 'some feedback into the ATO Call Centres but any complaints could not proceed until the tax file number (TFN) is reactivated via the Compromised TFN Unit.'<sup>189</sup>

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184 ATO, 'Office Minute (30 January 2012)', internal ATO document, p 1.

185 Ibid, p 2

186 ATO, 'Refund Fraud Hobart' (undated), internal ATO document.

187 ATO, 'Office Minute', above n 184, p 2.

188 ATO, 'Office Minute' (30 January 2012), internal ATO document, p 1.

189 Ibid, p 4.

4.122. In discussions with the IGT, ATO senior management have stated that operations such as the ones discussed above were successful in containing the GST fraud risks which had been identified. This has manifested in GST refunds not being issued erroneously and ATO's actions or decisions not being challenged.

4.123. Notwithstanding the success of the operations, in late 2012, the ATO augmented the procedures which guided the above operations through the addition of an addendum which required ATO officers to:

- attempt to contact the affected taxpayer;
- use both information provided upon the allocation of the case to them as well as other relevant information to determine the action required; and
- exercise judgment in deciding the final outcome based on all information available as well as the significance of the risk and the consequences of the decision.<sup>190</sup>

4.124. The ATO's objective was to ensure all affected taxpayers were contacted and given the opportunity to address any deregistration or refund cancellation concerns. Reinstatement of their registrations or issue of refunds would be provided upon the taxpayer satisfying proof of identity requirements or upon receipt of relevant supporting evidence. Instructions were also provided in the addendum for the ATO officer to provide contact details to assist the affected taxpayer in addressing the compromised TFN issues through the ATO's Client Identity Incident Management (CIIM) team and Client Identity Support Centre.<sup>191</sup>

4.125. As part of the current IGT review, the ATO has provided further information in relation to its current approach to potential identity fraud cases:

*When identity fraud is believed to have taken place, the ATO's Client Identity Support Centre will make contact with the client. After establishing their identity through the Proof of Record Ownership process, the ATO will ask a series of questions to determine whether it was the client that lodged the return. Where it's identified as identity fraud, the ATO will invite the client to register for voice authentication for additional protection, and will apply a range of safeguard measures to ensure the client's ATO record is protected from any future fraud attempts. The ATO will cancel any fraudulent lodgments, refunds and contact information, and invite the client to lodge their legitimate return. The ATO will provide advice on protecting their personal identity information and will advise that additional monitoring will occur over future lodgments.*

*The ATO will advise the client they can also contact IDCARE, who has partnered with the ATO to provide clients affected by Identity theft with a toll-free national identity security counsellors service on 1300 432 273 (more information on IDCARE at [www.idcare.org](http://www.idcare.org)).<sup>192</sup>*

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190 ATO internal email dated 8 November 2012.

191 Ibid.

192 ATO, 'ATO's management of GST refunds in cases involving suspected identity fraud', June 2016, internal ATO document, p 3.

4.126. Importantly, the ATO further explained that:

*The treatments applied to prevent further identity crime enabled refund fraud do not impact on the broader refund integrity suite of models or processes.*<sup>193</sup>

4.127. Specifically, all lodged BASs which claim refunds are subject to automated risk assessment tools that identify potentially incorrect or fraudulent refund claims, regardless of whether the taxpayer has a potential identity fraud indicator or is on a watch list for similar risks. Any BAS identified as being incorrect or potentially fraudulent is then referred to a specialist team that addresses both refund fraud and potential identity fraud.

4.128. As discussed in Chapter 4, the ATO's management of fraud and fraud-related risks within the GST context is set out in the RI Auditor Guide<sup>194</sup> and the ITX guidelines.<sup>195</sup> Both provide overarching guidance on management of suspected identity fraud, including reference to the Law Administration Practice Statement PSLA 2008/11 *Fraudulently altered or created income tax returns or activity statements*.<sup>196</sup>

4.129. As noted earlier, in 2016 the ATO undertook an internal Business Improvement Review in relation to refund fraud management. While the report did not specifically mention handling of identity fraud as an enabler for refund fraud, it does note that there is a discrepancy between the numbers of cases identified by the ATO's risk assessment tools (900 in income tax and 348 in indirect tax for the 2014-15 financial year) and potential identity fraud referrals from members of the public (25,658).<sup>197</sup> It also stated that the two avenues for identifying fraud were separate but complimentary. Although no recommendations were made in respect of process improvements on the treatment of identity fraud, the ATO stated that:

*Smarter Data is researching online behaviours with a view to detecting risk exposure prior to the actual fraud event (refund claim). This approach aims to improve client experience by detecting identity crime at the earliest possible point in the process, so that clients can be protected at the earliest opportunity.*<sup>198</sup>

## IGT Observations

4.130. Given the seriousness of the above allegations, the IGT considered them both at the time that they were raised and in more detail in the context of the current review. It is important to note that the same allegations were also directly conveyed to ATO management who seem to have acknowledged the concerns raised. In response, the

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<sup>193</sup> Ibid, p 3.

<sup>194</sup> ATO, 'RI Auditor Guide', above n 53.

<sup>195</sup> ATO, 'Indirect Tax guidelines for dealing with suspected fraud', 20 September 2017, internal ATO document.

<sup>196</sup> ATO, *Law Administration Practice Statement PSLA 2008/11 Fraudulently altered or created income tax returns or activity statements* (2015).

<sup>197</sup> ATO, 'Business Improvement Review', above n 86, p 12

<sup>198</sup> Ibid, p 13.

ATO explained that additional procedures had been added to augment the streamline processes used in operations such as Whip or Cohort.

4.131. It seems that taxpayers, affected by the above operations, were provided very limited information and were effectively required to contact the ATO to find out and address any actions that may have been taken against them. Although such situations are far from desirable and raise serious concerns, only a finite group of taxpayers, who were suspected of being involved in fraud, were affected for a limited period of time. Furthermore, these taxpayers could have approached the ATO or, at the time, the Commonwealth Ombudsman, to report their concerns. In the materials made available to the IGT, there were almost no instances of such reporting.

4.132. More importantly, the ATO appears to have addressed the above concerns in 2012 through the additional procedures discussed earlier. The materials provided to the IGT as part of the allegations made as well as other information provided by the ATO do not indicate that the practices in question are continuing. It should also be noted that the IGT has also not received any submissions or complaints indicating that such practices are still in place.

4.133. In the broader context of this review, the ATO has sought to continue improving its ability to detect instances of identity fraud through internal reviews and enhancements of the risk assessment tools, as discussed in Chapter 3. The IGT has also made recommendations for further improvements in this regard. Nevertheless, automated risk assessment tools will never be absolutely accurate and there is a risk of compliant taxpayers being selected for review or audit. In such cases, it is important that these taxpayers have effective avenues through which to raise their concerns and have them addressed. Such avenues are currently available through the ATO's CIIM team as well as the IGT's complaints handling service.



## CHAPTER 5 - IMPACTS ON TAXPAYERS

5.1. This chapter examines the impacts that the ATO's retention of GST refunds, and associated verification activities, may have on affected taxpayers and the options available to mitigate them.

### STAKEHOLDER CONCERNS

5.2. The impacts of the GST refund retention on taxpayers are generally financial in nature. Delays with obtaining refunds, which are due and payable, affect taxpayers' cash flows, operations and profitability, particularly where they are in low margin industries. This concern is a common thread that runs through most of the GST refunds complaints and stakeholder submissions that the IGT has received. Additional compliance costs, such as providing further information to the ATO or disputing its actions or decisions, may impose further financial burdens.

5.3. Stakeholders recognise that interest is payable to taxpayers after the statutory period to process a refund expires.<sup>199</sup> However, concerns have been raised that these amounts are trivial compared to the costs to taxpayers of having their refunds withheld. In the absence of refunds, taxpayers may incur financing costs if funds have to be borrowed to fulfil their obligations of paying other creditors. In some cases, they may face difficulties borrowing funds from financial institutions due to disclosures having to be made about any relevant ATO audit activity. In these circumstances, affected taxpayers may have to resort to personally injecting additional capital or rely on family and friends where this is an option.

5.4. Stakeholders have cited certain examples of refunds having a direct impact on the profit margins of taxpayers working in the property development industry, where transactions are often highly geared, and more reliant on external finance. Similarly, the delayed release of refunds can also lead to lost opportunities where those funds are required to carry out planned business transactions. One taxpayer indicated that his business was forced to delay \$20 million in exports due to the ATO's retention of refunds, amended assessments and audit actions.

5.5. Stakeholders have also raised a range of concerns regarding the ATO's consideration of the 10 statutory factors discussed in the previous chapter. This chapter explores in further detail one of these 10, namely, the requirement for ATO officers to consider 'the impact of retaining the amount on the entity's financial position'.<sup>200</sup>

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199 ATO, *Delayed refund of a Running Balance Account (RBA) surplus* (26 May 2016) <<https://www.ato.gov.au/>>.

200 *Taxation Administration Act 1953*, s 8AAZLGA(2)(c).

5.6. The following examples, drawn from complaints received by the IGT, illustrate how the above concerns arise:

- one taxpayer reported incurring over \$100,000 in legal fees disputing ITCs amounting to \$200,000 through a lengthy objection process;
- another taxpayer also incurred significant professional fees over an 18 month period in which the ATO undertook a GST refund audit; and
- within the agribusiness industry some concern was raised that refund verification delays were affecting farmers' ability to feed their livestock.

5.7. The financial impacts of the refund retention may also affect taxpayers' emotional and mental health. For example, a director of a business taxpayer has described to the IGT how the retention of refunds and ensuing audit had caused her depression and given rise to suicidal thoughts for which she is taking ongoing medication. Another taxpayer had been affected by fire destroying his farmland, assets and tax records while also dealing with a marriage breakdown. As a result, he had lodged multiple income tax returns and BASs late. Although he had received some assistance from the ATO with the lodgment of these returns, he had experienced significant delay in obtaining his GST refunds. This delay had severely impacted his already fragile emotional and mental health.

5.8. Stakeholders have noted that personal impacts are not specifically included within any of the 10 statutory factors. However, some stakeholders have suggested these personal factors should be taken into account under paragraph s8AAZLGA(2)(j) of the TAA 1953 as 'any other relevant matters'.

5.9. Lastly, there were certain concerns raised regarding taxpayers' access to compensation under the Scheme for Compensation for Detriment caused by Defective Administration (CDDA). The ATO's administration of the CDDA Scheme and broader related concerns were previously considered in an earlier IGT review, the *Review into Taxpayers' Charter and Taxpayer Protections*.<sup>201</sup>

## ATO MATERIALS

### Serious financial hardship

5.10. Taxpayers who are experiencing serious financial hardship may apply in writing to have their circumstances considered by the ATO and to request the expedited release of their GST or other refunds.

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201 IGT, *Taxpayer Charter and Taxpayer Protections* (2016).



5.11. For business taxpayers the ATO defines serious financial hardship as:

*... when an entity that requires their refund to continue their business for example pay staff wages, purchase essential supplies etc.*

*Factors contributing to serious hardship generally include family tragedy, financial misfortune, impacts of natural disaster and other serious or difficult circumstances. Other factors, for example: serious illness may be taken into consideration.<sup>202</sup>*

5.12. Furthermore, the ATO's website includes the following information regarding businesses experiencing serious financial hardship:

*Serious financial hardship can also apply to businesses that need their refund to continue business. Serious hardship means financial difficulty associated with:*

- *business closure*
- *disconnection of an essential service*
- *repossession of a vehicle used for business purposes*
- *imminent legal action pending for non-payment of debts*
- *period of review limitations*
- *court orders*
- *settlements*
- *other necessities for the business or people you are responsible for.*

*If none of these factors apply to your circumstances, you are unlikely to qualify for priority processing under serious financial hardship.<sup>203</sup>*

5.13. The ATO requires taxpayers to provide evidence of their hardship, which demonstrates their serious and immediate financial need.

5.14. In a GST refund verification context, the ATO provides a range of guidance to its officers as discussed in Chapter 4. Whilst circumstances such as insolvency, bankruptcy and 'other ATO work is in progress' are listed as scenarios where release of refunds should be considered, financial hardship is not mentioned.<sup>204</sup>

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202 ATO, 'Hardship actioning guidelines', 12 May 2016, internal ATO document.

203 ATO, *Businesses with Serious Financial Hardship* (6 April 2017) <<https://www.ato.gov.au/general/financial-hardship/Businesses-with-serious-financial-hardship/>>.

204 ATO, 'Early Exit Decision' (18 May 2017) internal ATO document.

5.15. However, taxpayers who are facing serious financial hardship may request for priority processing of their BAS.<sup>205</sup> Such requests are referred to the Client Account Services (CAS) business line. The ATO does not provide timeframes for the consideration of hardship applications nor does it provide an estimate as to when taxpayers can expect their GST refunds if their application is successful. It simply states that 'the ATO will endeavour to release the refund as soon as possible'.<sup>206</sup>

5.16. The ATO has not reported on taxpayer hardship applications since the 2013-14 financial year at which time, of the 2,400 hardship applications that had been received, 1,170 were found to be eligible for urgent processing.<sup>207</sup> No further breakdown is provided as to the number or proportions that relate to business or GST refunds. Accordingly, it is impossible to determine how many such applications have been lodged and how many have been successful in the GST refund context.

5.17. The ATO's consideration of hardship in GST refund cases is further complicated by the overarching need to consider the 10 statutory factors mentioned earlier. Specifically, the ATO has advised that:

*If a refund verification case work has been generated, a finding of financial hardship does not guarantee the refund will be released. The taxpayer's financial hardship is one of the factors the case officer will have regard when making a decision whether or not the refund is retained for verification.*<sup>208</sup>

5.18. Consistent with this approach, the ATO's general call centre scripting also advises that an active audit will have an impact on the request for urgent processing of the refund.<sup>209</sup>

5.19. In relation to the potential personal impacts, the ATO has published a list of health and wellbeing support organisations on its website.<sup>210</sup> However, it does not go further in detailing if and how these impacts would be considered within a hardship context. Furthermore, the ATO also publicly advises that these impacts are generally excluded from compensation, when considering claims of legal liability or applications under the CDDA scheme.<sup>211</sup>

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205 ATO, *Requesting Priority Processing* (6 April 2017) <<https://www.ato.gov.au/general/financial-hardship/requesting-priority-processing/>>.

206 ATO, 'HRDSHP0208I Requesting priority processing', 31 August 2017, internal ATO document.

207 Commissioner of Taxation, *Annual Report 2013-14* (2014) p 41.

208 ATO, *Commissioner's discretion to retain a refund*, above n 40, para 7; ATO, *Communication with the IGT* (8 August 2017).

209 ATO, 'HRDSHP0208I Requesting priority processing', above n 206.

210 ATO, *Health and wellbeing organisations* (6 April 2017) <<https://www.ato.gov.au/>>.

211 ATO, *Applying for compensation* (31 August 2016) <<https://www.ato.gov.au/>>.

## PSLA 2012/6 and paragraph 8AAZLGA(2)(c) of the TAA 1953

5.20. PSLA 2012/6 provides guidance on how ATO officers should consider the impact of retaining the refund on a taxpayer's financial position<sup>212</sup> as required by paragraph 8AAZLGA(2)(c) of the TAA 1953. PSLA 2012/6 only requires the consideration of this factor if financial hardship is specifically raised by taxpayers.<sup>213</sup> It also states:

*Information relevant to this factor may include evidence of financial hardship suffered by the taxpayer (whether an individual or corporate), such that it would compromise the taxpayer's business viability. Relevant evidence may include material provided by the taxpayer and relevant information otherwise available. [ATO officers] should evaluate the taxpayer's financial position and the impact of a retention decision on their immediate cash flow, solvency and borrowing needs. The size of the amount claimed may also be a relevant consideration in the context of particular taxpayer circumstances. However, the mere fact that a taxpayer will be deprived of a refund will not be a determinative factor against it being reasonable to retain an amount for verification.*<sup>214</sup>

5.21. As noted in Chapter 4, ATO officers may document their consideration of the 10 statutory factors in three ways. Where the Word template is used, the checkboxes available in respect of financial impact are:

- this has not been discussed with the taxpayer or their representative;
- the taxpayer or their agent has not indicated that retaining the refund will impact on their financial position; and
- taxpayer has indicated that retaining their refund will impact on their financial position.<sup>215</sup>

5.22. Although there is room for free text on the template, it is not mandatory for the officer to provide any further comment. The officer's ultimate decision as to whether the refund will be released, after considering the relevant factors, is simply recorded against one of the two checkboxes below:

- based on the above information it has been decided to retain the RBA Surplus; and
- RBA Surplus not retained, escalate to post issue.<sup>216</sup>

<sup>212</sup> ATO, *Commissioner's discretion to retain a refund*, above n 40.

<sup>213</sup> Ibid, para 8, example 9.

<sup>214</sup> Ibid, appendix.

<sup>215</sup> ATO, '10 Factors Worksheet', above n 130.

<sup>216</sup> Ibid.

5.23. In the Excel spreadsheet template, free text fields are available with the following guidance provided for all 10 factors:

*Based on a collective consideration of the 10 factors, assess the risk to revenue versus the client's entitlement to the refund. Where the risk to revenue is considered to outweigh the client's refund entitlement, the decision is made to retain the refund. Conversely, where the risk to revenue is not considered to be significant when assessed against other factors in favour of the client's entitlement to the refund, the decision must be made to release the refund. This assessment must be recorded in the ATO Position cell below the 10 factors for each Case Review and 60-day Case Callover held.<sup>217</sup>*

5.24. There are no separate instructions or guidance in respect of the financial impact on taxpayers. Two options are provided for the final ATO decision, both of which appear to favour retention of refunds:

*These factors indicate that the refund should be retained while further verification activities are conducted.*

OR

*Having considered all factors, it has been decided to retain the refund for verification.<sup>218</sup>*

## Partial release

5.25. The relevant Explanatory Memorandum for section 8AAZLGA of the TAA 1953, states that 'the amount the Commissioner may decide to retain could be part of the refund rather than the whole amount'.<sup>219</sup>

5.26. The RI Auditor Guide makes no direct reference to partial refund release but does refer to the internal FAQs<sup>220</sup> which state:

*[T]here are no automated business systems to enable the release of a partial refund and releasing a partial refund involves issuing a manual refund cheque. The processing and issuing of a manual cheque is labour intensive and involves an accounting integrity risk. Currently, manual refund cheques are only processed and issued in exceptional circumstances.<sup>221</sup>*

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217 ATO, 'Instructions on how to complete the 10 factors worksheet' (26 October 2016), internal ATO document.

218 ATO, '10 Factors Worksheet', above n 130.

219 Explanatory Memorandum, House of Representative, Tax and Superannuation Laws Amendment (2012 Measures No. 1) Bill 2012, p 76 para 7.30.

220 ATO, Commissioner's discretion to retain a refund – FAQ, above n 107, p 10.

221 Ibid.

5.27. The ATO had recognised the above systems limitations in 2012, shortly after section 8AAZLGA of the TAA 1953 had come into force. Internal advice from its Tax Counsel Network (TCN) noted:

*We understand that there are currently system limitations which would prevent, or at least make it very cumbersome, to release part of a refund claimed by an entity. These limitations may be regulated to some extent once a credit from a notification is posted to an account.*

*We consider that section 8AAZLGA will in most cases still support the retention of the full amount of the refund if the conditions that allow retention are satisfied. However, the balance of factors may more readily support the release of the remainder of the amount of the refund once the Commissioner becomes satisfied that the application of the law to the entity's circumstances would partly support the amount claimed by the entity. This is particularly so as the proportion of the amount that is considered properly payable increases.*

*While understanding the difficulties presented by the system limitations, we think it would be desirable for us in the longer term to prioritise system changes that would allow for greater flexibility in this regard. Allowing for partial release of refunds would provide benefits for the community in terms of accommodating cash flow. It would also assist in protecting the refund integrity system, as courts and tribunals may well be unsympathetic to the current limitations, and require us to release the full amount of a refund when it is still reasonable to verify information in relation to part of the claim.<sup>222</sup>*

5.28. Aside from the materials noted above there are no specific instructions for partial refund release and no further guidance on what ATO officers should consider to be an 'exceptional circumstance' warranting partial release.

## Interest on delayed refunds

5.29. The entitlement of taxpayers to interest for delayed refunds is established by section 12AA of the *Taxation (Interest on Overpayments and Early Payments) Act 1983*.

5.30. Interest is calculated and paid by reference to the Running Balance Account<sup>223</sup> and no discretion is applied in determining the amount.<sup>224</sup> The rate at which the delayed interest is payable is drawn directly from the base interest rate, as determined each quarter from the Reserve Bank of Australia published rates for the average yield for 90 day Bank Accepted Bills.<sup>225</sup> By comparison, the general interest charge on unpaid tax debts is seven percentage points higher than the base interest rate.<sup>226</sup>

<sup>222</sup> ATO, TCN Law Design Team Advice, 6 July 2012, internal ATO document, p 16-17.

<sup>223</sup> Used by the ATO to record liabilities and payments made on a single account for each taxpayer.

<sup>224</sup> *Taxation (Interest on Overpayments and Early Payments) Act 1983*.

<sup>225</sup> *Taxation Administration Act 1953* s 8AAD(2).

<sup>226</sup> *Taxation Administration Act 1953* s 8AAD(1).

5.31. The ATO reports interest paid on delayed refunds in its GST Administration Performance Annual Report 2015-16. For the three financial years between 2013-14, 2014-15 and 2015-16, the amount of interest paid had risen consistently from \$2.6 million to \$3.8 million.<sup>227</sup> The ATO attributes such increase to 'paying additional interest on settlements'.<sup>228</sup>

5.32. It should be noted that where taxpayer information contained in the BAS is incorrect or further information is required to process the BAS or the refund, the ATO is not required to pay interest on the delayed refund.<sup>229</sup> Examples of this would be where bank account details have not been provided to the ATO or where the taxpayer has outstanding BASs.

## IGT OBSERVATIONS

5.33. The ATO's retention of taxpayer refunds, even for short periods, may have a significant financial impact on taxpayers with follow on emotional and mental consequences. Conversely, early release of refunds adversely impacts government revenue where it is subsequently found that they should not have been paid and by that stage are not easily recoverable. The tension between these competing interests led *Multiflex*<sup>230</sup> to take legal action for the release of its refund and the Government to subsequently enact specific power for the Commissioner in the form of section 8AAZLGA of the TAA 1953. However, the latter contains safeguards for taxpayers such as requiring the Commissioner to consider the impact of retaining refunds on their financial position.

5.34. Interestingly, the use of refund retention as a fraud prevention measure has not been well received by the community. In 2011, the ATO commissioned TNS Social Research to conduct independent research over a 5 year period to gauge community perceptions regarding GST voluntary compliance. One of the matters explored was the community's views on delaying refunds as a fraud prevention measure. The report of that study, released in 2015, stated:

*Strategies suggested to aid in fraud prevention, such as delaying refunds and supplying additional information were not considered viable options for fraud prevention. It was thought that the amount of information provided to the ATO was sufficiently comprehensive and detailed and that further information would be unlikely to aid in fraud prevention. Delaying refunds to allow more time for the ATO to detect fraud received mixed reviews. For some, if the timeframe was communicated it would be acceptable, but for many, it was seen as an unnecessary threat to cash flow.*<sup>231</sup>

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<sup>227</sup> ATO, *GST administration performance annual report 2015-16*, above n 52, p 2.

<sup>228</sup> Ibid.

<sup>229</sup> ATO, *Law Administration Practice Statement PSLA 2011/23 Credit interest*, para 64.

<sup>230</sup> *Commissioner of Taxation v Multiflex Pty Ltd* [2011] FCAFC 142.

<sup>231</sup> TNS Social Research, *GST Compliance Research Program – Phase 5* (2015) pp 8-9.



5.35. As stated earlier, taxpayers who experience serious financial hardship, as a result of the GST refund verification being carried out, do have the option of lodging a hardship application and/or seeking partial release. However, it is difficult to gauge their awareness of these options as the ATO does not have any tracking or reporting mechanism in this regard.<sup>232</sup>

5.36. The IGT believes that the ATO should reinstate its reporting of hardship cases and expand it to provide more specific information that reveals the impact of some of its actions, such as retaining of refunds, as well as how it affects different types of taxpayers, particularly micro and small businesses.

5.37. The IGT is also of the view that more should be done to raise taxpayers' awareness that financial hardship applications may be, or indeed should be, lodged in appropriate cases. As business tax debts are not generally able to be released,<sup>233</sup> these taxpayers may not be aware that hardship needs to be proactively raised with ATO officers to ensure it is considered. As part of this review, the IGT examined 40 randomly selected GST verification cases to consider whether financial impacts had been considered by the ATO officers. None of these cases demonstrated such consideration being undertaken. This further highlights the need for greater awareness on the part of taxpayers and tax practitioners to proactively raise issues of financial hardship with ATO officers.

5.38. The ATO's template notification letters to taxpayers, currently, do not raise financial hardship at all. The IGT believes that these letters should inform taxpayers of options available to them if they are experiencing financial hardship. Where no letter is required to be issued, call centre scripting as well as website materials should similarly inform taxpayers.

5.39. As mentioned earlier, the IGT also considers that ATO officers should improve the documentation of their consideration of the 10 statutory factors contained in section 8AAZLGA of the TAA 1953. This is particularly important given that ATO officers have to exercise a degree of judgment and be mindful of the competing impacts on government revenue and taxpayers' cash flow. This is particularly so in the case of the paragraph 8AAZLGA(2)(c) of the TAA 1953, being the main factor which favours the taxpayer.<sup>234</sup>

5.40. Partial release of refunds also requires greater attention and improvement in order to alleviate any adverse financial impact on taxpayers. Although not generally promoted or actioned by the ATO, it does appear in the relevant legislative materials and the ATO's own advice and guidance. The only reason cited by the ATO for not making greater use of it is the administrative difficulties in doing so without the support of automated business systems.

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<sup>232</sup> ATO, Communication with the IGT (8 August 2017).

<sup>233</sup> ATO, *Debt relief, waiver and write off*, PSLA 2011/17, 29 August 2016, para 2.

<sup>234</sup> *Taxation Administration Act 1953* s 8AAZLGA(2)(f),(j); ATO, *Commissioner's discretion to retain a refund*, above n 40.



5.41. The IGT considers that the administrative difficulties cited are insufficient to reject requests for partial release of refunds. The manual processing of partial refunds may be difficult but it is also necessary to support the community and, as flagged by the ATO's own Tax Counsel Network, address the risk of adverse judicial findings against the ATO if these matters are challenged.<sup>235</sup> The IGT acknowledges that an automated system for partial release of refunds would be more desirable than a manual approach.

5.42. In addition, there would be benefits in the ATO raising awareness and providing further guidance in relation to the partial release of refunds to taxpayers as well as its own officers. This is especially important for taxpayers experiencing financial hardship or where the risks identified by the ATO only apply to a portion of the refund claimed.

5.43. In relation to interest on delayed refunds, the concerns related to the sufficiency of these interest payments as a form of compensation for the delay. The IGT has previously considered similar concerns in other reviews and, where appropriate, made recommendations for improvement.<sup>236</sup>

#### **RECOMMENDATION 5.1**

*The IGT recommends that the ATO:*

- (a) *improve access to and raise awareness of taxpayers, tax practitioners and its own officers about assistance available in serious financial hardship cases including full or partial release of GST refunds;*
- (b) *ensure that the appropriate consideration of the financial impact on taxpayers, as required by paragraph 8AAZLGA(2)(c) of the TAA 1953, and serious financial hardship claims are carefully documented; and*
- (c) *develop an automated system for the partial release of GST refunds.*

#### **ATO RESPONSE**

##### **(a) Disagree**

The ATO is committed to ensure taxpayers, their agents and staff, have access to and are aware of, the assistance that can be provided in situations where a taxpayer is suffering from serious financial hardship.

The ATO currently provides guidance in PSLA 2012/6 *Exercise of Commissioner's discretion to retain a refund* to taxpayers, their representatives and ATO staff in considering the impact of retaining a refund on the taxpayer's financial position. However, the impact on the taxpayer's financial position is one of 10 factors that need to be considered when making a decision to retain a refund.

<sup>235</sup> ATO, TCN advice, 22 November 2012, internal ATO document, p 5.

<sup>236</sup> See for example: IGT, *Review into improving the self-assessment system* (2012) pp 118-121; IGT, *Review into the Australian Taxation Office's administration of penalties* (2014), p 41.

The ATO website also has information on 'serious financial hardship' which includes what is considered to be serious hardship. Further information on serious financial hardship can also be found in PS LA 2011/17 *Debt relief, waiver and write off*.

**(b) Agree**

ATO case officers are required to document their decision to retain a refund after consideration of all 10 statutory factors in s8AAZLGA(2)(c) of the TAA 1953. We are currently developing additional training for staff to reinforce that all factors are considered and carefully documented, particularly in relation to the impact of retaining the refund on the client's financial position.

**(c) Disagree**

Due to system limitations, it is not possible to automate partial release of refunds. The ATO has the ability to partially release refunds via a manual process which is considered adequate considering the very limited situations where a partial release of refund is required.

The ATO can only retain a refund until it would be no longer reasonable to verify the information or has sufficient information to make an assessment.



## CHAPTER 6 - REFUND VERIFICATION IN THE PRECIOUS METALS INDUSTRY

6.1. The prior chapters of this report have considered the ATO's general process for verification of GST refunds pursuant to section 8AAZLGA of the TAA 1953. The ATO adopts more intensive approaches in respect of certain higher risk industries such as property development, agribusiness and precious metals. Complaints received by the IGT indicate that more recently the precious metals industry was the most affected by such approaches.

6.2. This chapter considers the ATO's approach to the precious metals industry as an illustration of how it addresses heightened risks and suspicions of GST refund fraud. The broader risk of GST non-compliance within the precious metal industry is being explored in another IGT review, namely the AFCM review.

### STAKEHOLDER CONCERNS

6.3. Stakeholders acknowledged that there are serious risks within the precious metals industry that have to be addressed. However, they believed that in addressing those risks, the ATO should minimise adverse impacts on those that are compliant.

6.4. The concerns that have been raised with the ATO's approach to GST refund integrity in the precious metals industry were largely similar but more acute than those already discussed in previous chapters. These concerns include:

- (a) undue delay in releasing refunds or issuing assessments, including many that had been retained by the ATO for over a year;
- (b) undue delay in issuing decisions on objections to the ATO's retention; and
- (c) a lack of transparency in the ATO's consideration of the 10 statutory factors and its disregard for the financial or personal impacts on affected taxpayers.

6.5. Stakeholders also question whether:

- (a) it is appropriate for the ATO to use a narrow provision, such as section 8AAZLGA of the TAA 1953, to undertake intensive audits to address 'industry-wide risks' of fraud in the supply chain involving third parties; and
- (b) section 8AAZLGA of the TAA 1953 appropriately addresses broader and serious compliance risks of this nature as the section raises expectations that either the ATO will release refunds or issue amended assessment while also being required to comply with a range of notification and other administrative tasks within short, specified timeframes.

## ATO MATERIALS

6.6. The ATO considers that the risks presented by certain participants within the precious metals industry are serious and, if not appropriately addressed, they have the potential to diminish confidence in the administration of the tax system. The seriousness of such risk was noted in an October 2016 bulletin issued by the Serious Financial Crime Taskforce, which comprises a range of law enforcement agencies such as the Australian Federal Police and the ATO:

*We are seeing sophisticated arrangements that attempt to obscure transactions of recycled 'investment form' precious metals.*

*We believe there are groups or networks of industry participants, including refiners, bullion dealers, gold kiosks, dealers and buyers within established supply chains involved in gold recycling (or carousel type) arrangements, seeking to exploit the GST rules in relation to precious metals.*

*These artificial arrangements are established to obtain a benefit from the tax system of which there is no entitlement and are tax crimes.<sup>237</sup>*

6.7. The ATO has also established a separate project team to review the transactions of the entire supply chains within the precious metals industry that give rise to ITCs and GST refunds. In this regard, the ATO has stated that:

*We maintained a strong focus on the deliberate and organised evasion of GST obligations within the gold bullion and precious metals refining industry as the evasive behaviour of taxpayers in this industry appears to be continuing. We have established some taxpayers are participating in a scheme. In one case, non-existent metal supplies were created in order to generate input tax credits from those supplies. Assessments were issued for \$122 million with additional penalties of \$58 million.*

*Our activities to mitigate this risk and deliver a fair and level playing field within this industry have so far raised around \$181 million in GST liabilities.<sup>238</sup>*

6.8. In addressing the risks within this industry, the ATO believes that it has done so in a manner which has not adversely impacted compliant taxpayers and has adhered to the requirements within section 8AAZLGA of the TAA 1953. Specifically, the ATO has advised that 14 taxpayers in the precious metals industry have been subjected to refund retention. Most of these taxpayers have common directors who had already been subject to compliance actions previously.

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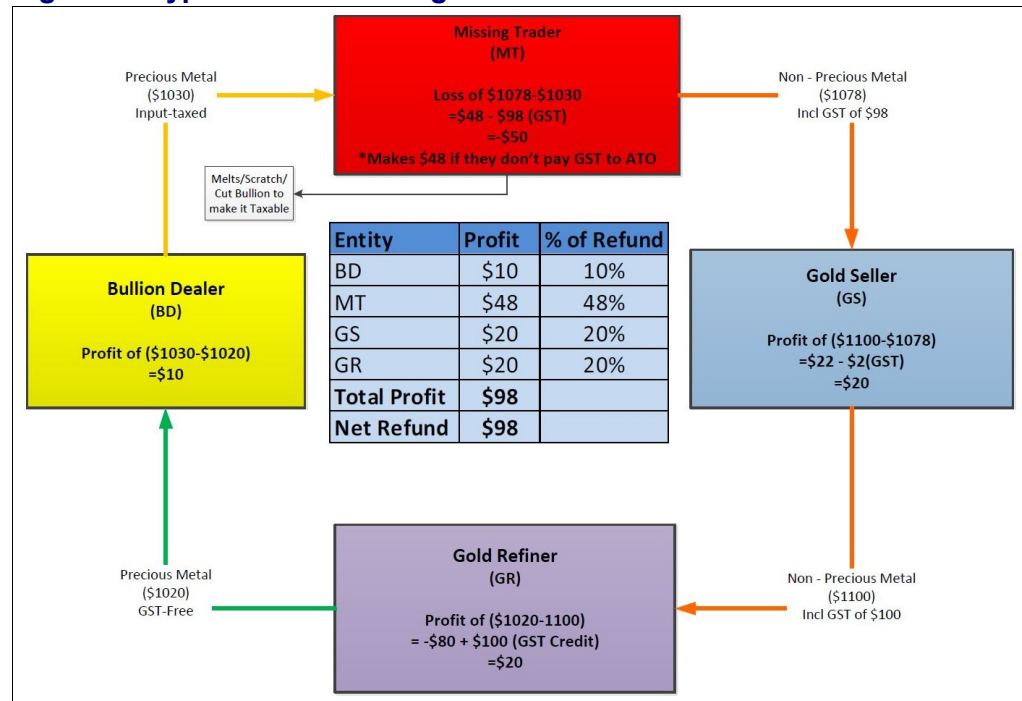
<sup>237</sup> Australian Federal Police, *Intelligence Bulletin: Targeting Fraud in the Precious Metals Refining Industry* (October 2016) <[www.afp.gov.au](http://www.afp.gov.au)>.

<sup>238</sup> ATO, *GST administration annual performance report*, above n 52, p 37.

## Risks within the precious metals industry

6.9. The ATO has explained by way of a hypothetical that the type of fraud it is seeking to address, called ‘missing trader fraud’, takes place through the series of transactions set out below in Figure 8.

**Figure 8: Hypothetical ‘missing trader’ illustration**



Source: ATO

6.10. **Stage 1:** The Missing Trader (red box) purchases gold bullion from a Bullion Dealer (yellow box) for \$1,030. It is treated as an input taxed supply of precious metal or is GST-free if it is the first supply following its refinement.<sup>239</sup>

6.11. **Stage 2:** The Missing Trader melts, scratches or cuts the bullion to make it taxable as scrap gold (as bullion must be pristine in order to retain its status as financial gold) and sells it to a Gold Seller (blue box) for \$1,078. GST attached to the transaction is \$98. The mischief arises where the Missing Trader does not lodge its BAS or remits the GST and, therefore, makes a profit of \$48. If the Missing Trader had lodged its BAS and remitted the GST, they would have made a loss of \$50.

6.12. **Stage 3:** The Gold Seller sells the scrap gold to a Gold Refiner (purple box) for \$1,100. The sale has \$100 GST attached to it which the Gold Seller remits. The Gold Seller is also entitled to a credit of \$98 (for the GST paid in Stage 2) and, therefore, remits a net amount of \$2, making a profit of \$20.

<sup>239</sup> A New Tax System (Goods and Services Tax) Act 1999 s 38-385.

6.13. **Stage 4:** The Gold Refiner refines the scrap gold and sells it as bullion for \$1,020 to the Bullion Dealer. This transaction is treated as first supply of bullion after refinement which is GST-free. The Gold Refiner is not required to remit any GST but is entitled to claim a credit of \$100 (for the GST paid in Stage 3). The credit offsets the loss of \$80 that would otherwise have been made and the Gold Refiner makes a profit of \$20.

6.14. The total loss of GST revenue to the Commonwealth from the above hypothetical transactions is \$98, which represents the \$100 refund received by the Gold Refiner (Stage 4) and the net GST of \$2 remitted by the Gold Seller (Stage 3). The cycle then commences again with the Bullion Dealer and Missing Trader transactions at Stage 1.

6.15. In October 2013, the ATO issued a press release announcing that it had jointly, with the Australian Federal Police and Australian Crime Commission, executed search warrants on premises associated with companies, operating in the precious metals industry, who were suspected of committing \$65 million in GST fraud.<sup>240</sup> Since that time, the ATO has observed that the attack on the revenue has escalated with more recent internal management reports noting that such loss is significantly higher with over \$700 million in primary tax having been raised.<sup>241</sup> In discussions with the ATO towards the end of this review, the IGT has been advised that the liabilities raised, inclusive of penalties, are \$905 million and likely to reach \$1 billion when all cases have been completed.

6.16. Pertinent to this review, the GST refund verification portion of the above fraud, that is the amount of refund withheld, totals \$2.4 million and \$21.5 million for the financial years ended 30 June 2016 and 30 June 2017, respectively. It should be noted that figures cited in relation to refund retention do not reflect the totality of the lost revenue arising from missing traders who have not remitted GST. The ATO estimates such amounts to exceed \$225m.

6.17. The current Australian experience in relation to the precious metals industry has parallels across similar jurisdictions. It is a risk that is apparent and managed by a range of different governments and revenue authorities.<sup>242</sup> The UK, Canada, New Zealand, Singapore, Malaysia, Germany and South Africa have all adopted different legislative and administrative processes for combatting such fraud. A summary table showing the comparative approaches adopted by these jurisdictions appear in Appendix 4.<sup>243</sup>

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240 ATO, *ATO investigates \$65m GST fraud in gold bullion trade* (Media Release 2013/33) <[www.ato.gov.au](http://www.ato.gov.au)>.

241 ATO, 'Commissioner briefing May 2017', internal ATO document.

242 Michael Walpole, 'Tackling VAT Fraud', *International VAT Monitor* (September/October 2014) pp 258-263.

243 ATO, Precious Metals Industry Improving Industry Compliance GST Options Paper (April 2017) internal ATO document.



6.18. It is noteworthy that ‘reverse charging’, as a means of combating the above fraud, was implemented by the UK in as early as 1993.<sup>244</sup> It was only introduced in Australia with an effective date of 1 April 2017. The reverse charge mechanism requires the purchaser to remit GST rather than the supplier.<sup>245</sup> In this way, by combining the purchaser’s right to claim ITCs with the supplier’s GST remittance payments, the transaction is neutral for GST purposes. This is achieved by the purchaser’s credit claim and supplier’s refund payments being set off by the supplier. The implications of the GST ‘reverse charge’ mechanism are considered in more detail in the AFCM review for the reasons noted earlier.

## Scope of the GST refunds retention provision

6.19. As the term ‘verification’ is not defined within the legislation, the intent has to be drawn from the Explanatory Memorandum which states:

*As the term verification is not defined, it (and the terms verify and verifying) is intended to take on its ordinary meaning. In the context of the provision, this could refer to actions or enquiries that may need to be taken to prove or establish the correctness or accuracy of the information provided.*

*The discretion is intended to allow the Commissioner to consider the correctness of the information provided by the taxpayer before refunding an amount the Commissioner would otherwise have to refund. It is not intended that the Commissioner use this discretion to withhold a refund merely where the Commissioner and the taxpayer disagree about how the law applies to the facts. The appropriate course of action for the Commissioner in these circumstances is to issue an assessment to reflect his or her view of the law.*<sup>246</sup>

6.20. The ATO is of the view that ‘verification’ may be applied to a broader range of considerations and investigations, rather than simply the immediate transaction that gives rise to the taxpayer’s GST refund claim. To date, there have been no judicial pronouncements on the scope of section 8AAZLGA of the TAA 1953.

## Audit and verification timeframes

6.21. The ATO’s timeframes for dealing with BAU GST refund cases were discussed earlier in Chapter 4. In comparison to those figures, the timeframes in precious metals cases are considerably longer. The ATO attributes the longer timeframes to the complexity of the arrangements and the number of entities within the supply chain. Table 7 below sets out the number of precious metal retention cases actioned in each of the 2015-16 and 2016-17 financial years.

<sup>244</sup> House of Lords European Union Committee, *Stopping the Carousel: Missing Trader Fraud in the EU* (25 May 2007) p 18.

<sup>245</sup> ATO, *Reverse charge in the valuable metals industry* (21 July 2017) <[www.ato.gov.au](http://www.ato.gov.au)>.

<sup>246</sup> Explanatory Memorandum to the Tax and Superannuation Laws Amendment (2012 Measures No 1) Bill 2012, p 75.

**Table 7: Overview of retention in precious metals industry 2015-16 and 2016-17**

	Year ending	
	30/06/2016	30/06/2017
Taxpayers with retained refunds	5	17
Number of BAS retained	19	45
<b>Total refunds claimed</b>	<b>\$2,452,918.00</b>	<b>\$21,503,593.00</b>
Released with adjustment	16	4
Release without adjustment	3	0
Still retained	0	41
<b>Total adjustments</b>	<b>\$18,572,873.30</b>	<b>\$7,716,468.00</b>

Source: ATO

6.22. As highlighted above, the number of BASs retained has increased across the two years. In 2015-16, a small fraction of BASs were released without adjustments, whilst the remainder contained not just denial of refunds but also included a large upward liability revisions from a total of \$2,452,918 net GST credit to an amended net GST liability assessment of \$18,572,873 (being a gross liability increase of \$21,025,791).

6.23. In the 2016-17 year, for the BASs where the ATO had retained the relevant GST refunds, none were released without adjustment and the majority remained outstanding.

6.24. The ATO's statistics in Table 8 show the time elapsed from case creation until finalisation (or the progress up to and including 16 November 2017) for cases within the precious metals industry.

**Table 8: Days elapsed – precious metals industry retention 2015-16 and 2016-17**

Entity	Case created	Case Finalised	Days elapsed
<b>Year ending 30 June 2016</b>			
Entity 1	7 October 2015	21 February 2017	503
Entity 2	6 October 2015	18 October 2016	378
Entity 3	16 December 2015	20 June 2016	217
Entity 4	7 September 2015	31 October 2016	420
Entity 5	14 October 2015	4 May 2017	568
<b>Average days elapsed</b>			<b>417.2</b>
<b>Year ending 30 June 2016</b>			
Entity 1	6 December 2017	N/A	N/A
Entity 2	13 October 2016	N/A	399
Entity 3	24 November 2016	N/A	357
Entity 4	6 September 2016	N/A	N/A
Entity 5	27 September 2016	N/A	415
Entity 6	31 January 2017	N/A	289
Entity 7	20 September 2016	N/A	N/A
Entity 8	9 June 2016	N/A	525
Entity 9	N/A	N/A	N/A
Entity 10	N/A	N/A	N/A
Entity 11	6 January 2017	N/A	304
Entity 12	23 November 2016	N/A	358
Entity 13	14 November 2016	N/A	367
Entity 14	10 January 2017	N/A	310
Entity 15	10 February 2017	N/A	279

Entity	Case created	Case Finalised	Days elapsed
<b>Year ending 30 June 2016 (continued)</b>			
Entity 16	10 May 2017	N/A	181
Entity 17	N/A	N/A	N/A
<b>Average days elapsed</b>			<b>344</b>

Source: IGT - Constructed from ATO source information.

Note 1: The retentions for entities 1, 4 and 7 have not been finalised.

Note 2: Entities 9, 10 and 17 have been flagged but no cases have been created.

Note 3: All remaining entities still have ongoing retentions. The days elapsed are calculated from the case creation date until 16/11/2017. The average is based only upon the days elapsed for entities where all relevant information was available.

Note 4: The above timeframes necessarily include periods during which the ATO issued and awaited the receipt of information from taxpayers.

6.25. Table 8 shows that in 2015-16, the average number of days elapsed between the ATO case creation and finalisation date for verification was 417.2 days. In the 2016-17 year, the ATO could only identify case creation dates for 11 of the 17 taxpayers. For those cases, the average number of days elapsed (having not yet been finalised) is 344 days as at 16 November 2017.

6.26. In respect of some of the cases with no finalisation date, in the above table, the ATO has advised the IGT that, even though amended assessments have been issued to those taxpayers, they remain open for operational reasons.

## Objections

6.27. As discussed in Chapter 4, although taxpayers have objection rights against the ATO's retention of GST refunds, it has not been widely used in the BAU context with only 3 cases being received between 1 July 2015 and 13 October 2017. In contrast, 24 objections have been lodged by precious metals taxpayers during the same period. Objections lodged by taxpayers are considered by officers within the Law Design and Practice Group of the ATO, separate from the Client Engagement Group which made the initial decision to retain the refund.

**Table 9: GST Retention of Refund Objections – 1 July 2015 to 13 October 2017<sup>247</sup>**

GST Retention of Refund objections	Precious Metals
Receipts	24
Allowed	0
Allowed in Part	0
Disallowed	20
Otherwise finalised (these objections became invalid prior to an objection decision issuing because of the release of the retained refund)	2
On hand as at 13 October 2017	2
Notices received pursuant to section 14ZYA of the TAA 1953	8
<b>TOTAL</b>	<b>24</b>

Source: ATO

6.28. Of the 24 objections received by the ATO, 20 were disallowed and 2 became invalid by reason of release of the refunds in question.

<sup>247</sup> ATO, Communication with the IGT, 20 October 2017.

6.29. Table 10 sets out the mean and median of time elapsed between receipt and issue of objection decisions for cases within the precious metals compliance project as at 13 October 2017.

**Table 10: Average time to complete precious metals refund retention objections**

Objections	Mean (days)	Median (days)
Finalised	136	128
On Hand	166	n/a

Source: ATO

Note: These times are calculated as at 13 October 2017.

6.30. Based upon the statistics provided by the ATO above, the average time taken to finalise an objection within the precious metals project is 136 days with a median of 128 days. Of those currently remaining on hand, the average time elapsed so far has been 166 days. The ATO considers this to be reflective of the complexity of the cases.

6.31. The ATO appreciates that an additional factor that may contribute to extended objection timeframes is the need for ATO officers to consider all relevant information available at the time a decision is made regarding the reasonableness of the retention. The information to be considered is not limited to that available at the date of the objection but includes additional information that becomes available later, for example as a result of an audit.<sup>248</sup>

## IGT OBSERVATIONS

6.32. The IGT, along with all stakeholders, acknowledge that there is non-compliant behaviour and serious risk of tax fraud in the precious metals industry and that these risks have to be addressed effectively without impacting compliant taxpayers.

6.33. In contrast to the BAU cases, the audit timeframes for the ATO's precious metals refund verification actions are more than 10 times longer on average and a larger proportion of affected precious metals taxpayers have exercised their rights to object. The consideration of the latter objections has taken longer than the ATO's prior service standard of 56 days<sup>249</sup> to finalise. It should be noted that, since 30 June 2016, the ATO has not set a service standard for its completion of any objection. Rather, the ATO has a range of service commitments in relation to resolving disputes, such as, to 'deal with the issue in a timely manner, seeking to understand and accommodate any issues of commercial urgency where possible'.<sup>250</sup>

<sup>248</sup> ATO, 'Objection to retention decision made under 8AAZLGA - information that an R&L officer may consider', internal ATO document.

<sup>249</sup> Commissioner of Taxation, *Annual Report*, above n 19, p 137.

<sup>250</sup> ATO, *Dispute or object to an ATO decision* (31 May 2017) <[www.ato.gov.au](http://www.ato.gov.au)>.

6.34. In audits and objections, relating to retention of refunds in the precious metal industry, examined by the IGT, the ATO has adhered to its obligations under section 8AAZLGA of the TAA 1953. However, certain practical difficulties in using provisions such as section 8AAZLGA of the TAA 1953 to address serious non-compliance risks have been identified in this review. As the ATO has observed in an internal briefing document:

*The efforts to retain refunds and contain revenue leakage are significantly limited by section 8AAZLGA of the Taxation Administration Act 1953, in particular the requirement that it must be 'reasonable' to retain the refund. The complex nature of the schemes means that there is insufficient time to make required enquiries prior to the release of refunds. It is not "reasonable" to retain a refund on a suspicion of tax avoidance or evasion alone, without evidence. Identifying and gathering evidence is made more difficult as WH&S [work health and safety] risks increase, and is also hindered where some of the participants have been drawn into schemes unknowingly.<sup>251</sup>*

6.35. Having considered both the taxpayer and the ATO positions, it appears that the fundamental problem is a mismatch between the expectations of both parties regarding the administration of these provisions.

6.36. On the one hand, the ATO has to conduct reviews and audits to fully explore, and where necessary prosecute, the issues under investigation, including undertaking enquiries of other parties in the supply chain which invariably requires significant time. It should also be noted that, as the ATO continues with such enquiries, further administrative time and costs will necessarily be incurred in reconsidering the requirements of section 8AAZLGA of the TAA 1953 as new information comes to light. Furthermore, the ATO also considers that their actions in addressing these refund risks need to take into account compliance behaviours, such as directors of taxpayers that have been subject to compliance action previously in respect of other entities under their directorship. Accordingly, the ATO believes these directors should be well aware of the risks sought to be addressed and processes involved.

6.37. On the other hand, taxpayers are expecting prompt processing of refunds based on their understanding of section 8AAZLGA of TAA 1953. Clearly, these expectations are not being met in some cases in the precious metal industry. Taxpayers may be labouring under a misapprehension that their case is a straight forward compliance check of the invoice(s) underpinning the claim. The idea that the retention process and audit process may be one and the same is not so well-understood by taxpayers who feel that they are being subjected to an inefficient audit process.

6.38. Although the ATO has indicated to the IGT that it has communicated its approach in this area through a range of channels, taxpayer complaints and submissions lodged with the IGT do not indicate that they had a clear understanding of the high level of risks sought to be addressed and the length of time required to finalise their particular case.

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251 ATO, 'Action Brief GST treatment of precious metals', 26 August 2016, internal ATO document, p 6.

6.39. The underlying cause for the lack of understanding or the mismatch in expectations appears to be the meaning of the word ‘verification’ in section 8AAZLGA of the TAA 1953. The Tax Institute and the Law Council of Australia, in their joint submission to Treasury on the initial drafting of this section, warned that the use of the word ‘verification’ could be read as setting a high forensic threshold. Accordingly, they submitted that a lower threshold should be set.<sup>252</sup>

6.40. Whether ‘verification’ encompasses a higher or lower threshold is ultimately a matter for the Tribunal and Courts to determine. However, such determination may be difficult given the challenges for taxpayers in raising objections or progressing further appeals as discussed in Chapter 4.

6.41. Whatever the outcome of a judicial pronouncement on the meaning of ‘verification’, it is clear from the foregoing discussion that there would be benefits in amending section 8AAZLGA of the TAA 1953 to allow the Commissioner to effectively investigate and address serious risk of fraud such as those currently in the precious metal industry. However, such exception to section 8AAZLGA of the TAA 1953 should only be triggered where serious risks of fraud are clearly established.

6.42. One option would be to require the ATO to seek a Federal Court order before it can classify a case as posing a risk of serious non-compliance with taxpayers being given the opportunity to contest such a classification if they have evidence to refute it. Some consideration should be given to cases where the ATO may need to take covert action. In those cases, the ATO could apply to the Court on an *ex parte* basis with taxpayers being notified after steps are taken to avoid prejudicing the investigation. At the time of such notification, taxpayers may become entitled to a right to seek judicial review. It should be noted that there is time and costs involved in seeking a Federal Court order.

6.43. Another option may be an approach akin to the ATO’s General Anti-Avoidance Rules (GAAR) Panel in which the ATO seeks advice from a panel comprising senior ATO staff as well as members from the private sector before GAAR is applied to a particular taxpayer. Given the nature of serious tax fraud risks and the cross-agency approach needed to combat them, it may be that the panel may also include senior officers from the AFP, Commonwealth Director of Public Prosecutions and other law enforcement agencies. However, this process may also be time consuming and costly. Furthermore, taxpayers and their representatives have raised concerns about aspects of the GAAR Panel process.<sup>253</sup>

6.44. The considerations about the ATO’s powers to combat serious risks within the tax system are pertinent beyond the current work in relation to the precious metals industry. Questions in this regard have been raised in a recent Treasury consultation paper, entitled: ‘*Combatting Illegal Phoenixing*’, where the ATO’s broader ability to retain refunds has been raised.<sup>254</sup>

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252 The Tax Institute and the Law Council of Australia, Consultation on Exposure Draft Legislation - Submission re proposed section 8AAZLGA of the Taxation Administration Act 1953 (22 February 2012) p 5.

253 IGT, *The Management of Tax Disputes* (2016) pp 45-46; IGT, *Work Program 2012-2013* (10 October 2012) <[www.igt.gov.au](http://www.igt.gov.au)>.

254 Department of the Treasury, *Combatting Illegal Phoenixing* (2017) p 32.

### **RECOMMENDATION 6.1**

*The IGT recommends that the Government consider amending section 8AAZLGA of the TAA 1953 to allow the Commissioner, in appropriate cases, to effectively investigate and address risks of fraud the seriousness of which has been established by means such as obtaining a Federal Court order.*

### **ATO RESPONSE**

Matter for Government





# APPENDIX 1 - TERMS OF REFERENCE

## BACKGROUND

The Goods and Services Tax (GST) was introduced in 2000 and is the largest source of taxation revenue after income tax.<sup>255</sup> The GST is economically borne by the final consumer but is collected and paid by businesses. Registered business taxpayers may claim input tax credits for the GST they have paid on any goods and services that they acquire. Such businesses are entitled to a GST refund where their input tax credits exceed the total GST charged by the business within a reporting period.

The Australian Taxation Office (ATO) is responsible for the administration of the GST including paying GST refunds,<sup>256</sup> the eligibility for which may be assessed before they are paid. Given the large number of refund claims, the ATO uses a risk-based approach to identify potentially incorrect or fraudulent claims. Such claims may be held back for checking by ATO officers and are only paid after their legitimacy or accuracy has been verified.

Historically, the ATO retained GST refunds, under its general powers of administration,<sup>257</sup> until verification checks were completed. However, in the 2011 *Multiflex*<sup>258</sup> case, the Full Federal Court ruled that GST refunds could not be retained any longer than the time needed to process the GST return. As a result, verification had to be conducted within a restricted period of time if it was to be done before refunds were issued. Following that decision, legislation<sup>259</sup> was enacted to allow the ATO to retain GST refunds for a longer period of time provided there were reasonable grounds to do so and the relevant taxpayer was notified within certain timeframes. Such taxpayers were also granted a right of review.

Stakeholders have indicated to the Inspector-General of Taxation (IGT) that, generally, the administration of the GST refund process works well. However, concerns have been raised with the GST refund verification process through the IGT's complaints handling service and in submissions to his current work program. These concerns include:

- a lack of clarity on the scope and nature of verification activities, including information requests;
- inadequate engagement with taxpayers and their representatives;
- inaccurate risk identification processes and inappropriate administration of the retention provisions including unexpected offsetting of GST refunds against future liabilities; and

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255 The GST amounted to 16.76 per cent (\$57.536 billion) of total net collections in 2015–16: Commissioner of Taxation, *Annual Report 2015–16* (2016) p 39; see also, Australian Bureau of Statistics, *5506.0 Taxation Revenue, Australia* (2016).

256 The ATO issued over 500,000 GST refunds in 2015–16, totalling \$54.169 billion: above n 1.

257 Section 356-5 of Schedule 1 to the *Taxation Administration Act 1953*.

258 *Commissioner of Taxation v Multiflex Pty Ltd* [2011] FCAFC 142.

259 Section 8AAZLGA of the *Taxation Administration Act 1953*.

- the adverse financial and emotional impact on taxpayers, particularly where the ATO does not fully appreciate their commercial arrangements as well as cash flow, working capital and profit margin implications.

This IGT review will consider the GST refund verification process, in particular the above concerns, in order to identify improvement opportunities which minimise adverse impact on taxpayers whilst ensuring that the ATO has sufficient time to adequately address risks to government revenue.

## TERMS OF REFERENCE

The IGT review into GST Refunds will focus on the GST refund verification process and in particular:

1. its accuracy in detecting incorrect or fraudulent claims;
2. engagement with affected taxpayers and their representatives throughout the process including timely notification of the retention, the reasons for it and rights of review as well as the appropriateness of any information requests and effectiveness of resolution mechanisms;
3. its interaction with other ATO compliance processes triggered due to other risks being identified or because the taxpayer is involved in certain industries;
4. the time required to conduct verification activities and opportunities to expedite the process through, for example, pro-actively providing information to the ATO; and
5. the impact on taxpayers and their representatives when considered against resulting adjustments, as well as the ATO's endeavours to minimise these impacts.

## SUBMISSIONS

The IGT invites you to make submission to this review. Please outline your experiences in dealing with the ATO together with any opportunities for improvement.

The terms of reference outlined above are designed to assist in structuring your submission. To further assist you in this regard we have included a list of questions below that may be helpful in formulating your submission.

### YOUR EXPERIENCE IN DEALING WITH THE ATO

1. *With respect to the retention of your GST refund:*
  - (a) *when and how were you first informed that your refund would be retained;*
  - (b) *how did the ATO engage with you or your representative throughout this process;*
  - (c) *were you provided with reasons for the retention of your refund and any proposed adjustments;*
  - (d) *how you were made aware of your rights of review in relation to the retention, as well as any adjustments;*

**YOUR EXPERIENCE IN DEALING WITH THE ATO (CONTINUED)**

- (e) *what actions did you take or information did you provide to assist the ATO in its verification; and*
- (f) *overall, how long did the ATO take to issue your refund?*
- (g) *Did the retention of your GST refund have an impact on you and/or your business? Please explain your answer.*
- (h) *Was interest paid for any time your GST refund was retained? If so, did you consider this amount reasonable? If not, what do you consider reasonable time-value for the money retained?*
- (i) *If you are a tax practitioner, has the retention of GST refunds had an impact on you or your practice in assisting your clients? Please explain your answer.*

**OPPORTUNITIES FOR IMPROVEMENT**

- 2. *Having regard to the possible risk to government revenue, how could the ATO best prevent GST refunds being issued for incorrect or fraudulent claims while minimising the impact on compliant taxpayers and their representatives?*
- 3. *Based on your experience, do you believe there are opportunities for the ATO to improve its approach to GST refund verification? Please explain your views.*

**Closing date**

The closing date for submissions is 17 May 2017. Submissions can be made by:

Post to:       Inspector-General of Taxation  
                   GPO Box 551  
                   SYDNEY NSW 2001

Email to:      gstrefunds@igt.gov.au

**Confidentiality**

Submissions provided to the IGT are maintained 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. Section 37 of the IGT Act safeguards the confidentiality and secrecy of such information provided to the IGT – for example, the IGT cannot disclose the information as a result of a Freedom of Information (FOI) request, or as a result of a court order generally. Furthermore, if such information is the subject of client legal privilege (also referred to as legal professional privilege), disclosing that information to the IGT will **not** result in a waiver of that privilege.



## APPENDIX 2 – MODEL STRIKE RATES FOR THE 2015-16 AND 2016-17 FINANCIAL YEARS

### ITX RIS Model performance 2015-16 – Client engagement program

ITX RIS Model Performance 2015-16 - Client Engagement Program													
Pre-Issue Cases Finalised FY 2015-16													
Model	Reviews	Audits	Total cases	Escalated reviews	Escalation rate	Adjusted reviews <sup>1</sup> (a)	Audit Outcomes <sup>2</sup> (b)	Total (a) + (b)	Strike rate on audits	Effective Strike Rate <sup>3</sup>	Revenue	Revenue per Outcome <sup>4</sup>	
SR MODELS		0	41	0	0.0%	0	30	30	73.2%	73.2%	\$372,501	\$12,417	
		0	16	0	0.0%	0	9	9	56.3%	56.3%	\$1,530	\$170	
		1	26	0	0.0%	0	14	14	53.8%	51.9%	\$134,551	\$9,611	
		235	168	142	60.4%	4	124	128	73.8%	49.0%	\$1,309,574	\$10,231	
		346	194	189	54.6%	5	151	156	77.8%	44.4%	\$3,243,720	\$20,793	
		580	522	323	55.7%	5	337	342	64.6%	43.9%	\$5,136,633	\$15,019	
		48	23	19	39.6%	3	18	21	78.3%	40.4%	\$220,410	\$10,496	
		91	57	35	38.5%	2	40	42	70.2%	37.2%	\$6,331,768	\$150,756	
		1749	1,007	1,012	57.9%	10	637	647	63.3%	37.1%	\$11,246,491	\$17,383	
		854	438	422	49.4%	10	304	314	69.4%	36.1%	\$2,425,578	\$7,725	
		0	3	0	0.0%	0	1	1	33.3%	33.3%	\$34,583	\$34,583	
		167	108	75	44.9%	2	63	65	58.3%	32.5%	\$337,660	\$5,195	
		288	139	137	47.6%	2	80	82	57.6%	28.3%	\$1,726,747	\$21,058	
		1780	825	804	45.2%	17	480	497	58.2%	27.6%	\$4,545,263	\$9,145	
		226	86	89	39.4%	2	59	61	68.6%	27.4%	\$620,282	\$10,169	
		140	56	54	38.6%	2	26	28	46.4%	19.7%	\$325,012	\$11,608	
		289	91	92	31.8%	3	51	54	56.0%	18.8%	\$796,296	\$14,746	
		170	61	53	31.2%	1	27	28	44.3%	15.7%	\$932,297	\$33,296	
		6,964	3,861	3,446	49.5%	68	2,451	2,519	63.5%	34.1%	\$39,740,896	\$15,776	

Note: Model names have been redacted as they provided descriptions of the models and inner workings which may be misconstrued or misused.

## ITX RIS Model performance 2015-16 – Client engagement program (continued)

	ITX RIS Model Performance 2015-16 - Client Engagement Program													
	Pre-Issue Cases Finalised FY 2015-16													
nRRE	Note: Model names have been redacted as they provided descriptions of the models and inner workings which may be misconstrued or misused.		99	75	174	52	52.5%	0	58	58	77.3%	47.5%	\$1,617,331	\$27,885
			29	22	51	20	69.0%	0	12	12	54.5%	38.7%	\$591,193	\$49,266
			95	38	133	35	36.8%	1	28	29	73.7%	29.6%	\$402,105	\$13,866
			193	82	275	78	40.4%	1	54	55	65.9%	27.9%	\$63,574,145	\$1,155,894
			133	59	192	55	41.4%	1	35	36	59.3%	26.3%	\$2,621,895	\$72,830
			3,147	1,152	4,299	1,139	36.2%	52	758	810	65.8%	25.6%	\$89,884,577	\$110,969
			561	148	709	154	27.5%	3	102	105	68.9%	18.9%	\$7,799,153	\$74,278
			4,553	1,258	5,811	1,311	0.0%	29	703	732	55.9%	16.3%	\$127,512,508	\$174,197
			145	37	182	38	26.2%	1	21	22	56.8%	15.3%	\$919,409	\$41,791
			285	73	358	71	24.9%	1	40	41	54.8%	14.3%	\$4,629,146	\$112,906
			6	3	9	2	33.3%	0	1	1	33.3%	14.3%	\$2,004,904	\$2,004,904
			27	7	34	4	14.8%	0	4	4	57.1%	13.3%	\$240,579	\$60,145
			2,657	600	3,257	645	24.3%	16	306	322	51.0%	12.3%	\$40,882,598	\$126,965
			333	38	371	46	13.8%	4	14	18	36.8%	5.5%	\$67,682,535	\$3,760,141
			0	1	1	0	0.0%	0	0	0	0.0%	0.0%	\$0	\$0
	12,263	3,593	15,856	3,650	29.8%	109	2,136	2,245	59.4%	18.4%	\$410,362,078	\$182,789		
Other		80	140	220	36	45.0%	3	98	101	70.0%	54.9%	\$10,103,072	\$100,030	
		115	227	342	60	52.2%	1	150	151	66.1%	53.5%	\$28,971,353	\$191,863	
		39	110	149	25	64.1%	0	64	64	58.2%	51.6%	\$552,937	\$8,640	
		0	6	6	0	0.0%	0	3	3	50.0%	50.0%	\$14,936	\$4,979	
		39	18	57	15	38.5%	0	7	7	38.9%	16.7%	\$37,306	\$5,329	
		273	501	774	136	49.8%	4	322	326	64.3%	51.1%	\$39,679,604	\$121,717	
Grand Total			19,500	7,955	27,455	7,232	37.1%	181	4,909	5,090	61.7%	25.2%	\$489,782,577	\$96,224

1 This represents the number of reviews with a financial outcome

2 Audit outcomes (i.e. strikes) includes financial and non- financial outcomes

3 Effective strike rate is the proportion of 'adjusted reviews and audit outcomes' over the 'total number of refund interventions'. The number of 'refund interventions' is calculated by 'total cases' less the number of 'escalated reviews'

4 This is calculated by dividing 'total revenue' by the number of 'adjusted reviews and audit outcomes'



## ITX RIS Model performance 2016-17 – Client engagement program

ITX RIS Model Performance 2016-17 - Client Engagement Program														
Pre-Issue Cases Finalised FY 2016-17														
Model		Reviews	Audits	Total cases	Escalated reviews	Escalation rate	Adjusted reviews <sup>1</sup> (a)	Audit Outcomes <sup>2</sup> (b)	Total (a) + (b)	Strike rate on audits	Effective Strike Rate <sup>3</sup>	Revenue	Revenue per Outcome <sup>4</sup>	
SR MODELS	Note: Model names have been redacted as they provided descriptions of the models and inner workings which may be misconstrued or misused.		0	6	6	0	0.0%	0	6	6	100.0%	100.0%	\$3,593	\$599
			227	198	425	145	63.9%	2	166	168	83.8%	60.0%	\$2,976,978	\$17,720
			367	189	556	195	53.1%	7	148	155	78.3%	42.9%	\$3,558,596	\$22,959
			458	280	738	242	52.8%	7	198	205	70.7%	41.3%	\$4,049,754	\$19,755
			1,478	891	2,369	822	55.6%	20	597	617	67.0%	39.9%	\$10,382,601	\$16,828
			680	341	1,021	324	47.6%	10	243	253	71.3%	36.3%	\$2,837,393	\$11,215
			194	87	281	88	45.4%	3	67	70	77.0%	36.3%	\$681,785	\$9,740
			346	171	517	175	50.6%	8	115	123	67.3%	36.0%	\$1,728,033	\$14,049
			254	128	382	126	49.6%	5	73	78	57.0%	30.5%	\$3,185,997	\$40,846
			1,220	545	1,765	522	42.8%	13	344	357	63.1%	28.7%	\$5,166,858	\$14,473
			438	152	590	164	37.4%	5	103	108	67.8%	25.4%	\$2,237,910	\$20,721
			191	65	256	63	33.0%	0	43	43	66.2%	22.3%	\$364,729	\$8,482
			21	10	31	8	38.1%	0	5	5	50.0%	21.7%	\$172,612	\$34,522
			44	11	55	17	38.6%	0	8	8	72.7%	21.1%	\$150,594	\$18,824
			103	39	142	41	39.8%	2	18	20	46.2%	19.8%	\$415,144	\$20,757
	6,021	3,113	9,134	2,932	48.7%	82	2,134	2,216	68.6%	35.7%	\$37,912,577	\$17,109		

## ITX RIS Model performance 2016-17 – Client engagement program (continued)

		ITX RIS Model Performance 2016-17 - Client Engagement Program												
		Pre-Issue Cases Finalised FY 2016-17												
nRRE	Note: Model names have been redacted as they provided descriptions of the models and inner workings which may be misconstrued or misused.		7	11	18	6	85.7%	0	8	8	72.7%	66.7%	\$331,675	\$41,459
			14	24	38	12	85.7%	1	16	17	66.7%	65.4%	\$570,484	\$33,558
			0	2	2	0	0.0%	0	1	1	50.0%	50.0%	\$920,554	\$920,554
			107	44	151	42	39.3%	0	30	30	68.2%	27.5%	\$4,723,728	\$157,458
			150	60	210	64	42.7%	2	38	40	63.3%	27.4%	\$8,438,017	\$210,950
			2,643	942	3,585	962	36.4%	47	663	710	70.4%	27.1%	\$78,696,974	\$110,841
			539	167	706	165	30.6%	6	103	109	61.7%	20.1%	\$4,256,489	\$39,050
			15	4	19	4	26.7%	0	3	3	75.0%	20.0%	\$84,540	\$28,180
			311	85	396	98	31.5%	4	54	58	63.5%	19.5%	\$7,698,259	\$132,729
			35	9	44	8	22.9%	1	6	7	66.7%	19.4%	\$251,876	\$35,982
			4,003	1,137	5,140	1,149	28.7%	30	677	707	59.5%	17.7%	\$67,226,193	\$95,087
			104	28	132	26	25.0%	0	17	17	60.7%	16.0%	\$863,680	\$50,805
			2,333	529	2,862	527	22.6%	17	269	286	50.9%	12.2%	\$25,970,908	\$90,807
			266	42	308	49	18.4%	4	19	23	45.2%	8.9%	\$38,484,483	\$1,673,238
			3	0	3	1	33.3%	0	0	0	0.0%	0.0%	\$0	\$0
			10,530	3,084	13,614	3,113	29.6%	112	1,904	2,016	61.7%	19.2%	\$238,517,860	\$118,312
Other		1	297	298	1	100.0%	0	257	257	86.5%	86.5%	\$4,743,198	\$18,456	
		78	107	185	40	51.3%	3	81	84	75.7%	57.9%	\$21,528,079	\$256,287	
		0	9	9	0	0.0%	0	5	5	55.6%	55.6%	\$11,463	\$2,293	
		42	31	73	19	45.2%	0	23	23	74.2%	42.6%	\$164,890	\$7,169	
		121	444	565	60	49.6%	3	366	369	82.4%	73.1%	\$26,447,630	\$71,674	
Grand Total			16,672	6,641	23,313	6,105	36.6%	197	4,404	4,601	66.3%	26.7%	\$302,878,067	\$65,829

1 This represents the number of reviews with a financial outcome

2 Audit outcomes (i.e. strikes) includes financial and non- financial outcomes

3 Effective strike rate is the proportion of 'adjusted reviews and audit outcomes' over the 'total number of refund interventions'. The number of 'refund interventions' is calculated by 'total cases' less the number of 'escalated reviews'

4 This is calculated by dividing 'total revenue' by the number of 'adjusted reviews and audit outcomes'

## APPENDIX 3 – ITX – RIA SERO MATRIX

### ITX – RIA Sero matrix - General

ITX - RIA Sero Matrix - General				
Sero Criteria	Sero Sub-criteria	Controls	Control Descriptors	Explanatory Notes
<b>Active Case Management</b> <i>Give clients what they need, when they need it, and in the form they want it. (C. Jordan)</i>	1. Taxpayer Engagement	Exp	It is clear that the taxpayer experience was positively enhanced during the Review/Audit	Evidenced through feedback received from the taxpayer. Evidenced in recorded discussions with the taxpayer and in case report notes.
		Yes	We have kept the Taxpayer informed in a timely manner	Have we kept the taxpayer informed of the progress of the Review/Audit? The auditor has clearly demonstrated that the taxpayer was kept fully informed of any delays in the actioning the case. If the case was unable to be finalised in a timely manner, are conversations documented noting any blockers discussed with the taxpayer. Was taxpayer provided with a new timeframe for finalisation of the case?
			The auditor has set appropriate expectations for the taxpayer	Taxpayer engagement should cover off on an explanation of the end to end process. Was the expected Audit completion date discussed and provided to the taxpayer? Is there evidence in the case report, on siebel or in letters to the taxpayer that set the expectation of when we anticipate to finalise the audit?
			We have tailored our communications to meet the taxpayer's needs	Was our communication with the taxpayer, clear and fit for purpose? For example, was the appropriate tone and language used in discussions with the taxpayer? Taking into account the different levels of understanding in relation to taxation matters, the officer is required to tailor their conversations to better ensure taxpayer understanding. Was information provided to the taxpayer in plain, easy to understand language. Are case notes written appropriately; in plain English and understandable?
			The appropriate method of taxpayer contact was used	Was initial taxpayer contact made by telephone? If unable to contact taxpayer by telephone were other communication avenues explored?
		No	One or more 'Yes' controls not satisfied	
		N/A	No Taxpayer Contact - Early Exit Case Only No Taxpayer Contact - Risk mitigated	No Taxpayer Contact - Early Exit Case Only While the Preferred Refund Integrity method is to contact the Taxpayer, in this case the risk has been mitigated.
	2. Active Case Management Principles Applied	Exp	Not an available option	The 'Exceptional' control is not available for selection under this sub-criterion
		Yes	The case was actively managed by the auditor	Has initial contact been made within 48 hours of case allocation? Are our communications with the taxpayer consistent without unnecessary/lengthy delays in responding to the taxpayer? Actively managing the case includes setting expectations with the taxpayer and effectively managing these with a view to continually progress the case to finalisation, this also includes engagement with the Audit Leader where appropriate.
			The auditor has followed case call over procedures	Has the auditor engaged with their Audit Leader early on in the case to ensure they are on the right track. Is there evidence of an ACM Siebel activity every 30 days?
			Requests for information were necessary and handled efficiently using the appropriate channels	There needs to be a valid reason for requesting the information. If yes, was the timeframe to comply reasonable? Was the request made in a timely manner? Was the most appropriate channel used (e.g. telephone, email)? Did we already have enough information to make a decision? For example, RP Data used instead of requesting documentation unnecessarily. Did we review the documentation for completeness in a timely manner? And if information missing did we request further documentation in a timely manner?
		No	One or more 'Yes' controls not satisfied	
		N/A	Not an available option	The 'Not /Applicable' control is not available for selection under this sub-criterion

## ITX – RIA Sero matrix – General (continued)

ITX - RIA Sero Matrix - General				
Sero Criteria	Sero Sub-criteria	Controls	Control Descriptors	Explanatory Notes
<b>Display Professionalism</b> <i>Provide a professional, client centric service, including use of correct channel and an educational component</i>	3. Educational Opportunities	Exp	Not an available option	The 'Exceptional' control is not available for selection under this sub-criterion
		Yes	We have provided education to the taxpayer when required	Did we provide education to the taxpayer when an opportunity presented. For example, did we provide education to the taxpayer on the correct classification of; Supplies or Acquisitions, or Tax Invoice Requirements, Attribution, Reporting - Cash versus Accruals, particularly relevant if an error was detected during the Review/Audit.
			We referred the taxpayer to self help options to assist in the prevention of future non-compliance	Where appropriate, have we educated the taxpayer on the availability of options such as, ATO website, mygov, ability to request private rulings to address their particular circumstances, availability of industry specific information on ato.gov.au, Small Business Newsroom etc.
		No	One or more 'Yes' controls not satisfied	
		N/A	Educational opportunities were not able to be offered to the taxpayer	Educational opportunities were not able to be offered to the taxpayer due to the taxpayers' existing level of understanding and/or knowledge of taxation matters and/or case was an Early Exit case
	4. Taxpayer Focus	Exp	The Auditor provided a level of service that exceeded the taxpayer's needs	Did the auditor go above and beyond what was required of them during the Review/Audit?
		Yes	We maintained a purposeful, respectful and professional relationship with the taxpayer	When explaining decisions to taxpayers, did the officer consider using the non-technical explanations available in the GST definitions published on our external website? Were our interactions meaningful with the taxpayer? Were our discussions relevant to the taxpayer?
			Interactions were made as easy as possible for the taxpayer	Has the Auditor obtained a thorough understanding of the taxpayers' business and taxation situation. Has the auditor tailored the request for information/documentation to meet the taxpayers' specific situation and appropriate to the risk. (i.e. not asking for 6 largest tax invoices as a default where they are not relevant to the risk)
			Where appropriate, Correcting GST Errors, Small Errors, Guiding Principles have been considered	Where appropriate, has Correcting GST Errors, Small Errors, Guiding Principles been considered?
			We have offered a service that meets the taxpayer's needs	Have we asked the taxpayer if there is anything else we could help them with? (Once and Done principles)
		No	One or more 'Yes' controls not satisfied	
		N/A	No Taxpayer Contact - Early Exit Case Only	No Taxpayer Contact - Early Exit Case Only
	5. Proof of Record Ownership (PORO) & Privacy Principles	Exp	Not an available option	The 'Exceptional' control is not available for selection under this sub-criterion
		Yes	PORO/POI satisfied	Proof of Record Ownership : Have details been checked and updated if appropriate?
			Privacy maintained	Privacy of the taxpayer was maintained. For example, no sensitive information was provided to a third party or unauthorised contact.
			Activities linked to correct taxpayer record/s	The officer must be sure they do not link activities or attach documents that do not relate to the taxpayer or the case.
		No	One or more 'Yes' controls not satisfied	
		N/A	No Taxpayer Contact - Early Exit Case Only	No Taxpayer Contact - Early Exit Case Only

## ITX – RIA Sero matrix – General (continued)

Sero Criteria	Sero Sub-criteria	Controls	Control Descriptors	Explanatory Notes
<b>Make Decisions</b> <i>Our responses display good research, risk consideration, decision making and are correct</i>	6. Determining and addressing the Risk	Exp	Not an available option	The 'Exceptional' control is not available for selection under this sub-criterion
		Yes	The risk has been appropriately identified	Based on the reason for case creation/profiling notes etc. has the auditor demonstrated a clear understanding of the risk? For example, identified recent bank account changes and/or Auskey changes, large capital acquisitions, unusual trading patterns, enterprise.
			The risk has been appropriately addressed	Did the auditor use appropriate mitigating strategies, for example, contacting the taxpayer to confirm if they changed the bank account etc. Have formal powers been used where information is not forthcoming? e.g Bank Notices, use of formal powers to obtain information etc.
			Where appropriate, the Auditor has identified any additional risks outside of the initial reason for case creation	Outside of the risk that generated the case being created, did the auditor identify the additional risk apparent from their audit. For example, associated third party risks, association with fraud groups, same tax invoice used/claimed multiple times by different entities etc.
			Where additional risks have been identified they have been appropriately addressed	Were additional risks identified addressed prior to case finalisation
		No	One or more 'Yes' controls not satisfied	
	7. Evidence, Intelligence and Escalations	N/A	Not an available option	The 'Not /Applicable' control is not available for selection under this sub-criterion
		Exp	Not an available option	The 'Exceptional' control is not available for selection under this sub-criterion
		Yes	Substantiation	Were independent third party checks adequately conducted and documented? Was tangible evidence of how the enterprise is funded received (where appropriate)? Has an actual supply occurred? For eg, what is the commercial reality of the transaction?
			The decision to internally escalate the case was correct	Has the auditor appropriately escalated the case? For example; to another area within the ATO such as Complex Assurance and Evasion, Business Assurance etc.
			The appropriate profiling system was used	Has the Auditor used the resources available to appropriately profile the taxpayer, including RAPT SNOOPY, RASS, Austrac data, RP Data, Mascot, etc?
			Intelligence has been appropriately referred	Has the Auditor completed the CDC which is required for every taxpayer? Where appropriate, has the Property tab been completed? Where appropriate has an ATOI been submitted? How accurate is the CDC data? Does the intelligence/information recorded make sense?
		No	One or more 'Yes' controls not satisfied	
		N/A	Not an available option	The 'Not /Applicable' control is not available for selection under this sub-criterion
	8. Correct decision	Exp	Not an available option	The 'Exceptional' control is not available for selection under this sub-criterion
		Yes	The compliance decision is correct	Is the decision defensible to external scrutiny? Was the advice provided technically accurate (based on legislation, rulings, determinations, ATO view etc.)? If Early Exit or low risk is the decision not to pursue documented and reasonable based on the information available? Is the decision well supported by appropriate evidence recorded in the case and/or supported by Correcting GST Errors, Small Errors Policy etc.
			The decision made was within the appropriate authorisation/delegation guidelines	The case officer has the appropriate authorisation/delegation to make their decision, or sought authorisation/delegation from a suitably qualified officer. If approval was provided by someone other than the case officer, were appropriate notes recorded in ATO systems?
			Penalties have been correctly considered and applied	The penalty decisions were correct in accordance with the case outcome. Safe harbour provisions have been considered and applied where applicable. Taxpayer behaviour (including any Voluntary Disclosures) have been appropriately considered. The penalty decision has been communicated to the taxpayer.
			Interest charges have been considered, communicated and correctly addressed	Where appropriate, interest charges have been correctly considered and applied to the taxpayers' account (including full remission, partial remission or full imposition) and have been communicated to the taxpayer.
		No	One or more 'Yes' controls not satisfied	
		N/A	Not an available option	The 'Not /Applicable' control is not available for selection under this sub-criterion

## ITX – RIA Sero matrix – General (continued)

Sero Criteria	Sero Sub-criteria	Controls	Control Descriptors	Explanatory Notes
<b>Be Accountable</b> <i>Our actions are accountable; ethically, administratively and in law</i>	9. Adherence to procedures and processes	Exp	Not an available option	The 'Exceptional' control is not available for selection under this sub-criterion
		Yes	For all pre-issue cases, the principles of s8AAZLGA legislation have been appropriately adhered to	Has the decision to retain a refund under s8AAZLGA been communicated to the taxpayer within the required timeframe?
			The 10 factors worksheet has been attached to the case and/or Siebel	Has the 10 factors worksheet been attached to the case and/or Siebel?
			The initial contact activity has been created in Siebel CCH screen by the Auditor	Has the initial contact activity been created in Siebel CCH screen by the Auditor?
			Voluntary Disclosure has been offered to the taxpayer and sufficient details recorded	Has follow-up questioning been appropriate to verify that it is a genuine disclosure? Does the disclosure satisfy all risks identified in the case, or is further risk mitigation required. For eg the disclosure relates to an amount reported but the inherent risk actually concern whether or not an enterprise exists.
			The auditor appropriately escalated the case from Review to Audit Product	Consider the reasons for escalation, ensuring there was an issue to pursue.
			The taxpayers records have been accurately and appropriately updated	Have the amendments to IPS been made correctly, do they match the case decision. If applicable are penalty amounts keyed into the system correctly?
			We tailored our approach and took into account individual circumstances	Did we 'make the call' early enough; including making decisions and applying sensible risk management?
		No	One or more 'Yes' controls not satisfied	
		N/A	Not an available option	The 'Not /Applicable' control is not available for selection under this sub-criterion
	10. Record management	Exp	Not an available option	The 'Exceptional' control is not available for selection under this sub-criterion
		Yes	Complete record of all internal and external interactions	Notes attached are clear, concise and accurate showing the interactions that took place with internal stakeholders and/or the taxpayer and decisions made. All relevant documents/emails are attached in Siebel correctly.
			Complete record of decision made	
		No	One or more 'Yes' controls not satisfied	
		N/A	Not an available option	The 'Not /Applicable' control is not available for selection under this sub-criterion



## APPENDIX 4 – JURISDICTIONAL COMPARISON TABLE

### JURISDICTIONAL COMPARISON TABLE

CRITERIA	AUSTRALIA	NEW ZEALAND	CANADA	UNITED KINGDOM	SINGAPORE
<b>'Precious metal' definition</b> <ul style="list-style-type: none"> <li>Type</li> <li>Fineness</li> </ul>	Gold (99.5% fineness) Silver (99.9% fineness) Platinum (99% fineness)	Gold (99.5% fineness) Silver (99.9% fineness) Platinum (99% fineness)	Gold (99.5% fineness) Silver (99.9% fineness) Platinum (99.5% fineness)	'Investment gold' refers to: <ul style="list-style-type: none"> <li>gold (99.5%)</li> <li>gold (post-1800)</li> </ul> 90% purity in/was legal tender in country of origin and price <180% spot price.	Gold (99.5% fineness) Silver (99.9% fineness) Platinum (99% fineness)
<b>Form requirements</b>	Required to be in an 'investment form' – in bar/wafer/coin, bears hallmark guaranteeing fineness and traded by reference to spot price.	Any form	In the form of a bar, ingot or wafer that must generally be recognized and accepted for trading on Canadian financial markets.  Coins: issued by a government authority and that may be used as currency will qualify.	Bar or wafer or a weight accepted by the billion markets. A coin that satisfies the legislative requirements.	Must be in a bar, ingot or wafer and possess 'investment characteristics'.  Coins must be listed in the GST Act to obtain concessional treatment.
<b>GST-free / Zero-rating</b>	GST-free on the first supply from refiner to dealers, input taxed on subsequent supplies.	GST-free on the first supply providing it is an ' <b>investment item</b> '.	the first sale of newly refined precious metal by the refiner or its owner is zero-rated (GST-free).	GST-free if acquisition is between Central Banks, or between a Central bank and LBMA member, or between LBMA members.	None
<b>Input taxed / GST-exempt</b>	All subsequent supplies of 'precious metals' are input taxed.	All subsequent supplies of 'precious metals' are input taxed in ' <b>any form</b> ' only.	Same as Australia	All transactions of investment gold are GST-exempt (unless it already meets GST-free requirements).	Supply of 'investment precious metal' (IPM) are generally GST-exempt (that is, meets the purity, form and accreditation requirements).
<b>Taxable</b>	Gold/silver/platinum that do not meet the definition of 'precious metal' are taxable (for example, alloy gold, not in investment form etc.)	Same as Australia	Same as Australia	Gold that are not GST-free or GST-exempt would be taxable.	Supplies of metals that do not meet the 'investment precious metal' definition are taxable.



**JURISDICTIONAL COMPARISON TABLE (CONTINUED)**

CRITERIA	AUSTRALIA	NEW ZEALAND	CANADA	UNITED KINGDOM	SINGAPORE
<b>Accreditation of refiners</b>	No accreditation is required.	None	Any person who in the regular course of business converts or refines gold, platinum or silver regardless of the degree of purity.	LBMA accreditation required (unless the party is a Central Bank).	LBMA accreditation LLPM accreditation Intends to be LBMA/LLPM accredited and endorsed by International Enterprise Singapore Board.
<b>Special rules on second-hand goods</b>	ITCs for acquisitions of second hand goods from unregistered entities for purposes of sale or exchange.	ITC not available for second-hand precious metal from unregistered dealers, but this is currently under review.	No ITCs available for acquisition of used goods after April 23, 1996	No special rule on acquisition of second hand precious metal.	No special rule on acquisition of second hand precious metal.
<b>Gold-bullion specific invoicing requirements</b>	None	None	None	None	Yes – IPM traders must supply within 30 days an invoice which names the supplier. The purchaser type of precious metal, weight, purity name of refiner, unique serial number, name and weight of coin, weight, total amount payable, etc.
<b>Registration / Notification / Reporting requirements to revenue authority</b>	None – no requirement to notify ATO of precious metal transactions.	None	None	HMRC needs to be notified within 28 days of making the first exempt supply of investment gold > £5,000 (or 12mth period > £10,000) (applies to both VAT-registered and non-registered entities). This is a one-off notification.	In order to access GST-exemption for investment precious metal, the entity must be an Approved Refiner and Consolidator Scheme (ARCS) entity.

Source: ATO

## 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

### Review into GST Refunds

Thank you for the opportunity to comment on your final draft report for your *Review into GST Refunds*.

As the report recognises, the vast majority of GST refunds are processed and released without being stopped for verification. We appreciate your acknowledgement in the report that the administration of the GST refund process is operating efficiently and of the work that is currently in progress to:

- further improve our risk assessment tools, and
- to streamline our processes and procedures associated with verifying GST refunds.

More specifically, your review has provided the opportunity to look at improvements to:

- the framework of continuous improvement for our risk assessment tools,
- our engagement with taxpayers, and
- how we consider and document our decisions to retain GST refunds.

We agree with 8 of the recommendations in the report, disagree with 5 of the recommendations and there is 1 recommendation which is a matter for government. In general terms, where we have disagreed with recommendations, this is due to practicalities associated with their implementation. Our detailed response to the recommendations is contained in Annexure 1.

We consider it is important to make some observations relating to that part of the report (Chapter 6) that deals with discrete aspects of the GST refund verification process within the precious metals industry. As you are aware, this is just one of the strategies we have employed to address the GST non-compliance that exists within that industry, and we acknowledge that the broader risk issues in this regard are being explored in the IGT's *Review into the ATO's Fraud Control Management*.

The ATO's view is that compliant taxpayers in the precious metals industry have not been impacted by the retention of refunds.

Many of the taxpayers involved in having their refunds retained have either present directors or associated entities previously involved in compliance action that relates to \$282 Million in primary tax assessments issued to date. Further, many of these entities have been liquidated by these directors leaving considerable debt to the Commonwealth.

The remaining taxpayers, while not subject to prior compliance action, have suspect supply chains and a number of missing traders resulting in significant risk to revenue. We note that the IGT has reviewed complaints by taxpayers who have not previously been subject to compliance action, and made no adverse findings in relation to these complaints.

Finally, I would like to acknowledge the efforts of all involved in undertaking this review.

If you require further information on our response, please contact Phillip Jones on (02) 9374 8365.

Yours sincerely



Neil Olesen  
Second Commissioner  
13 March 2018

## SHORTENED FORMS

Abbreviation	Meaning
AAT	Administrative Appeals Tribunal
ABN	Australian Business Number
AFCM	ATO's Fraud Control Management
ARCS	Approved Refiner and Consolidator Scheme
ASR	Actual Strike Rate
ATO	Australian Taxation Office
ATOi	ATOintelligence
AUSTRAC	Australian Transaction Reports and Analysis Centre
BAS	Business Activity Statement
BASE	BAS Engagement
BAU	Business As Usual
CAC	Client Account Centre
CAS	Client Account Services
CCD	Case Context Documents
CDC	Case Data Capture
CDDA	Compensation for Detriment caused by Defective Administration
CERIC	Client Engagement Risk Investment Committee
CIIM	Client Identity Incident Management
CISC	Client Identity Support Centre
EBR	Expert Business Rules
EDN	Export Declaration Number
FAQ	Frequently Asked Questions
FTE	Full Time Equivalent
GAAR	General Anti-Avoidance Rules

Abbreviation	Meaning
GPO	General Post Office
GST	Goods and Services Tax
HMRC	HM Revenue and Customs
ICP	Integrated Core Processing
IGT	The Inspector-General of Taxation
INS	Insolvency
IPS	Instalment Processing System
ITC	Input Tax Credit
ITX	Indirect Tax
LBMA	London Bullion Market Association
LPPM	London Platinum and Palladium Market
N10	Import Declaration Form
OBC	Online BAS Check
OESR	Outcome Effective Strike Rate
PGE	Public Groups Assurance and Engagement
PSLA	Law Administration Practice Statement
R&L	Review and Litigation
RAPT	Risk Assessment Profiling Tool
RBA	Running Balance Account
RI Auditor Guide	Refund Integrity Auditor Guide
RIA	Refund Integrity Assurance
RICP	Refund Integrity Case Processing
RoRA	Retention of Refund Analyser
RRE	Risk Rating Engine

Abbreviation	Meaning
SR	Suspect Refund
TAA 1953	<i>Taxation Administration Act 1953</i>
TCN	Tax Counsel Network
TFN	Tax File Number
TRG	Telephony Reference Group
UK	United Kingdom
VAT	Value-Added Tax
WH&S	Work Health and Safety