

PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

Taxpayer Engagement with the Tax System

House of Representatives Standing Committee on Tax and Revenue

August 2018
CANBERRA

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Foreword

In this inquiry, the Committee examined the Australian Taxation Office's points of engagement with taxpayers and other stakeholders, and reviewed its performance against advances made by revenue agencies in comparable nations.

The first thing to emphasise is that 'taxpayer engagement' in the current century is not what it was twenty years ago. Digitisation of tax lodgement processes, of financial interactions and information, as well as budget pressures have made it into a different business for governments and taxpayers. Tax administration has become a 'service', with automated systems designed to both reduce the compliance burden and to boost revenue collection up front.

This report provides a thorough review of progress in Australia's tax administration systems against this background. However, it also goes beyond that to ask what taxpayers should now expect from a modern tax service which is largely or partly automated.

The terms of reference for the inquiry were very broad. The first opened the inquiry wide by bringing in the issue of taxpayer non-engagement. This meant reviewing approaches used to attack the black or cash economy, here and overseas. Another theme was how the enterprise of tax compliance could be aided by the new behavioural economics insights (BEI) approach, using digital tools or 'nudges' to make it easier for taxpayers to comply, and harder not to.

During the inquiry, the Committee received extensive evidence from the ATO about its 'reinvention' as a modern automated tax administration system—to deliver reliable and intuitive online systems, to increase cyber-

security and taxpayer confidence in its fairness and facilities. This evidence gave much to be confident about.

However, the inquiry also raised alarms which the Committee was compelled to explore. In particular, the Committee was concerned that complexity in Australia's tax system is impeding the ATO's transformation into a fully automated and intuitive service.

Australia's complex system for claiming workplace related deductions, for example, was highlighted during the inquiry as being out of step with approaches in most other advanced nations, which had almost universally standardised their approach. It was noted that Sweden, the United Kingdom and, closer to home, New Zealand, with simpler tax policy in this area, have moved faster to fully automated or 'push return' tax systems where few taxpayers have to lodge a form.

The Committee concluded that, under Australia's self-assessment model, more should be done to make tax obligations easier for taxpayers to understand and simpler to comply with.

The Committee has made 13 recommendations in this report to achieve this goal. The first recommendation calls for a complete review of the tax system by 2022, to reduce complexity and to make it both easier to enforce and to understand.

The Committee also recommends for more immediate tax reform to close up tax loopholes, and to meet new challenges evolving with the increase in freelance and contracting work. In particular, it calls for introduction of a standard workplace expenses deduction scheme, where a standard deduction applies unless fully substantiated claims are made, and consideration of a new graded ABN withholding tax system, akin to the model introduced in New Zealand.

Other recommendations go to improve the amenity of automated tax systems to assist taxpayers and reduce error. This includes monitoring outcomes for BEI trialling approaches to ensure these methods and tools are genuinely effective and 'give more tax revenue for the taxpayers' buck'.

Finally, if there could be any doubt, this inquiry has confirmed that digitisation of tax services is the 'silver bullet' to new and traditional problems of tax administration around the world.

The Committee recognises the drivers, including the financial imperatives. However it also holds concerns that some Australians are not ready for the

transition—either through lack of opportunity, poor online access, or concerns about cybersecurity or privacy of personal information.

The Committee firmly believes that taxpayers have a right to exercise individual freedom of choice to meet their tax obligations, and should be able to do so by various mechanisms. Continued access to paper format tax returns and information at the myGov Shopfront is an important commitment here.

Finally, it is a fact that, in the 21st century, modern tax administration involves many partners—tax office professionals and outsourced staff, other government agencies, software designers and telcos, enforcement agencies and banks, as well as taxpayers, tax professionals and other intermediaries.

Taxpayers must have reliability in tax services and an unimpeded choice of tax service provider within this ‘eco-system’ of tax engagement.

To support this important principle, the Committee calls on the ATO, as a priority, to implement a service level agreement with stakeholders affected by the ATO’s changing practices, in particular tax agents who, at the coal face in the tax industry, experience delays during business peaks in activity.

The Committee also recommends that the ATO conducts a comprehensive review of its high level mission statements to devise a single, cohesive and easily understood framework—‘a regulatory philosophy’, that *clearly and simply outlines* the rights and obligations of both the Tax Office and taxpayers in the tax engagement process.

Accountability is the key to confidence. The Committee believes that implementation of these measures will demonstrate the ATO’s commitment to both fairness and efficiency as its digital transformation evolves.

Jason Falinski MP

Chair

September 2018

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Abbreviations

Anti-Money Laundering and Counter-Terrorism Financing (regime)	AML/CTF
Application Programming Interfaces	APIs
Attorney-General's Department	AGD
Australian Business Number	ABN
Australian Bureau of Statistics	ABS
Australian Competition and Consumer Commission	ACCC
Australian Community Attitudes to Privacy Survey	ACAPS
Australian Cybercrime Online Reporting Network	ACORN
Australia's Future Tax System (review)	AFTS
Australian Institute of Company Directors	AICD
Australian National Audit Office	ANAO
Australian Prudential Regulation Authority	APRA
Australian Public Service Commission	APSC
Australian Retailers Association	ARA
Australian Securities and Investments Commission	ASIC
Australian Taxation Office	ATO
Base Erosion and Profit Shifting (project)	BEPS
Behavioural Economics Team of the Australian Government	BETA
Behavioural Insights Team (United Kingdom)	BIT

Behavioural Insights Unit (NSW Government)	BIU
Business Activity Statement	BAS
Capital Gains Tax	CGT
Chartered Accountants Australia and New Zealand	CAANZ
Civil Aviation Safety Authority	CASA
Commonwealth Public Sector Union	CPSU
Common Reporting Standard	CRS
Department of Prime Minister and Cabinet	PM&C
Digital Transformation Agency	DTA
Document Verification Service	DVS
Federal Tax Service (Russia)	FTS
Financial technology	Fintech
Goods and Services Tax	GST
Gross Domestic Product	GDP
Her Majesty's Revenue and Customs (United Kingdom)	HMRC
High Net Wealth Individuals	HNWIs
Information and communications technology	ICT
Inland Revenue Service (United States)	IRS
Inspector-General of Taxation	IGT
International Funds Transfer Instructions	FTIs
Institute of Public Accountants	IPA
Know Your Client	KYC
Master Grocers Australia	MGA
National Identity Proofing Guidelines	NIPGs
New Payments Platform	NNP
New Zealand Inland Revenue	NZIR
Office of the Australian Information Commissioner	OAIC
Organisation for Economic Co-operation and Development	OECD
Personal Services Income (rules)	PSI

Pay As You Go	PAYG
Reserve Bank of Australia	RBA
Royal Melbourne Institute of Technology	RMIT
Self-managed super funds	SMSF
Signal Touch Payroll	STP
Standard Business Reporting	SBR
Superannuation Guarantee	SG
Swedish Taxation Authority	STA
Reserve Bank of Australia	RBA
Tax File Number	TFN
Value Added Tax	VAT

Members

Chair

Mr Jason Falinski MP	Mackellar, NSW
(Continuing Member and Chair from 28 March 2018)	
Mr Kevin Hogan MP (to 26.03.18)	Page, NSW

Deputy Chair

Ms Julie Owens MP	Parramatta, NSW
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Members

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Mr Milton Dick MP	Oxley, QLD
Ms Nicolle Flint MP	Boothby, SA
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Terms of Reference

The Committee will inquire into how taxpayers, particularly individuals and small businesses, engage with Australia's tax system and examine opportunities to improve this experience through the greater use of information technology, automated and natural systems, and 'nudges'.

As part of this inquiry, the Committee will examine:

- The prevalence and impact of the 'cash economy' on the tax system, mechanisms to ensure tax compliance and strategies used by comparable countries' revenue authorities;
- how taxpayers currently interact with the tax and superannuation system, including through tax agents and other intermediaries, and the different compliance burdens of doing so;
- the contemporary use of information and communication technology by the Australian Taxation Office and comparative tax administrators to deliver services; and
- behavioural insights from other service delivery agencies including possible ways to better inform taxpayers to help them make decisions in their best interests.

Explanatory Paper—supporting the terms of reference

In 2010, Australia’s Future Tax System Review Report (the AFTS review) envisaged a 21st century tax system that would allow taxpayers to engage with it in ways that meet their needs and preferences.¹ Since then, changes to technology and reporting regimes have allowed taxpayers to start receiving a more contemporary service.²

This inquiry provides an opportunity to explore in detail how different types of taxpayers, particularly individuals and small businesses, currently engage with Australia’s tax system and how they might like to do so in the future. This can help inform the Government’s longer term policy agenda.

It may also provide insights in how to respond, in both policy and administrative terms, when taxpayers deliberately choose not to engage with the tax system.

In undertaking this inquiry, the Committee may wish to have regard to the following framing questions and issues.

How do taxpayers currently engage?

- What do taxpayers perceive they need to do (or think they need to do) to comply with their obligations? What informs these views?
- How do different taxpayers manage their affairs? Do they choose to engage tax advisers and other intermediaries³ and, if so, what are their reasons for doing so?
- Are there any broader trends emerging from specific taxpayer experiences?

¹ See the discussion in Chapter G4 in the Final Report from Australia’s Future Tax System Review.

² The ATO is currently undertaking a range of research projects that may be of interest to the Committee, see: <www.ato.gov.au/about-ato/research-and-statistics/current-research-projects/>

³ For example, as of 30 June 2016, there were 75,436 registered tax practitioners in Australia.

How could taxpayers engage in the future?

- How do other tax systems operate⁴ and how do they compare to Australia?
- Do other service delivery organisations (including overseas tax authorities) provide any particular behavioural insights (fairness, social norms and group effects) that could be adapted to the tax system?

How does this best inform a longer term policy agenda?

- How would potential changes fit within the existing tax system? Are there any broader sensitivities, impediments or other changes that need to be in place first?
- Who would carry the compliance burdens and who would receive the compliance benefits? Are there ways of minimising these costs?⁵

⁴ For example, see Her Majesty's Revenue and Customs (HMRC), 'Making Tax Digital' 2015.

⁵ For example, see the discussion in paragraphs 4.3-4.10 in the explanatory memorandum to Tax and Superannuation Laws Amendment (2015 Measures No 5) Bill 2015 and the discussion (Context of amendments) in Chapter 23 of the explanatory memorandum to Budget Savings (Omnibus) Bill 2016.

List of Recommendations

Recommendation 1

3.179 The Committee recommends that a review of Australia’s tax system should be undertaken before 2022, with the purpose of making recommendations on how to simplify the present tax system, in order to reduce both the quantum of tax law and improve comprehension and compliance by people without expertise in taxation law.

Recommendation 2

4.35 The Committee recommends that the ATO should continue to deploy behavioural insights approaches to increase taxpayer engagement. The ATO should, however, examine and report on the results of these programs or activities, recognising their limitations within an overly complex tax system.

Recommendation 3

4.38 The Committee recommends that the ATO should make greater use of behavioural insights techniques, such as randomised controlled trials, before full implementation of new initiatives to determine if such changes are indeed better than current practices, and if so, which changes are the most effective.

The ATO could also run continuous trials (using methodology such as, but not limited to, the Lean Six Sigma system¹) on communication platforms and

¹ Six Sigma is a disciplined, data-driven approach and methodology for eliminating defects (driving toward six standard deviations between the mean and the nearest specification limit) in any process – from manufacturing to transactional and from product to service. See Six Sigma <www.isixsigma.com/new-to-six-sigma/getting-started/what-six-sigma > viewed 24 July 2018.

channels to ensure that its systems are constantly being tested and improved.

Recommendation 4

- 4.54 The ATO consider adopting a Regulatory Philosophy to codify the principles on which it will administer tax laws and engage with taxpayers.

Recommendation 5

- 4.128 The Committee recommends that the ATO should continue to expand availability of technical initiatives such as pre-filing, simplified electronic lodgement systems for business and individuals, and online assessment tools to facilitate Australia's transition to a 'push return' tax system.

While supporting these developments, the Committee upholds the individual's choice to manage their own tax affairs, using ATO or commercial products, and to seek professional advice from tax professionals enabled by efficient online lodgement services.

Recommendation 6

- 6.24 Based on the New Zealand system, the Committee recommends that Treasury considers an ABN withholding tax system at source for all industries with the potential for the rates to be industry specific.

Recommendation 7

- 6.27 The Committee recommends the ATO should review the functionality of the contactor assessment tool for accuracy and utility to taxpayers by reference to the functionality of the tool deployed in the United Kingdom, and report to the Committee on its progress.

Recommendation 8

- 6.45 The Committee recommends that the work-related deductions scheme be reformed by introducing the standard deduction concept as proposed by the Australia's Future Tax System Review.

Fairness would be maintained by enabling individuals to claim above the set amount by providing full substantiation through a tax return process.

Recommendation 9

- 6.69 The Committee recommends that the ATO should adopt a roadmap for the abolition of paper-based returns, including testing and trialling with user groups.

Recommendation 10

- 6.70 For the foreseeable future, the Committee recommends that the ATO maintain paper-based returns and the distribution of paper publications on request to those people who choose to engage this way.

Additionally, taxpayers seeking non-digital tax resources for tax returns at a myGov Shopfront should be assisted on site.

Recommendation 11

- 6.121 In the interests of promoting fairness and taxpayer confidence in Australia's tax system, the Committee recommends that the ATO should work to develop a framework which clearly outlines the rights and obligations of both parties in the tax engagement process for adoption in the near future.

The process, involving the review of high level ATO mission statements, would be consistent with the ATO's principle-based approach to service delivery and support design of a Regulatory Philosophy document.

Recommendation 12

- 6.122 The Committee also recommends that, in implementation and change management programs, the ATO should include a service level agreement with end users, especially tax agents, that includes amongst other things, consideration of payments to end users for poor delivery outcomes.

This is proposed in recognition that the ATO is a monopoly provider that is not subject to contestability in its service delivery.

Recommendation 13

- 6.124 The Committee recommends that the ATO should engage with all service providers according to the principle of competitive neutrality, allowing taxpayers the ultimate choice of which channel of access or service to use, and which channel is in their best interests.

1. Conduct of inquiry

Role of the Committee

- 1.1 The primary role of the House of Representatives Standing Committee on Tax and Revenue is parliamentary scrutiny of federal tax administration. Prior to the 44th Parliament this function was conducted by the Joint Committee of Public Accounts and Audit, including, since 2007, through biannual reviews of the Annual Reports of the Commissioner of Taxation. These recurrent reviews continue to be conducted under Standing Order 215(c) which authorises the Committee to examine the annual reports of agencies allocated to it by the Speaker.¹ In addition, the Committee may receive a ministerial referral to investigate areas of tax and revenue policy. The Committee also has the capacity to request the Inspector-General of Taxation, under section 8(3)(d) of the *Inspector-General of Taxation Act 2003*, to undertake aspects of inquiry into the tax system.²

¹ The Speaker's Schedule of Annual Reports, presented 15 September 2016, allocates scrutiny of the Australian Taxation Office, as well as other agencies, including the Treasury, to the Committee. The annual report review function has been conducted annually since 2017.

² The Inspector-General of Taxation (IGT) is not obliged to comply with the request. During the Committee's inquiry into tax disputes the Committee focussed on small to medium enterprises and individuals and asked the IGT to conduct a similar inquiry into large taxpayers and high wealth individuals. The IGT agreed to do so and the Committee's report referenced the IGT report which was provided to the Assistant Treasurer and tabled in Parliament. Refer: House Standing Committee on Tax and Revenue, *Tax Disputes*, March 2015, p. xiv.

Inquiry overview

- 1.2 On the 25 November 2016 the Committee adopted the terms of reference provided by the Minister for Revenue and Financial Services, the Hon Kelly O'Dwyer MP. The full terms of reference are detailed at the front of this report, along with an explanatory paper provided by the Treasury in support of the terms of reference. Both the terms of reference and the explanatory paper were published to the Committee's website.
- 1.3 The scope of this inquiry was limited by nature of the role of the Committee—and through the terms of reference—to the prevailing and emerging taxation environment and tax administration within that context. The Committee has received high level commentary about taxation policy, most comment supporting policy streamlining; with reference to simplification as raised in Australia's Future Tax System Review (the AFTS review).³
- 1.4 The Committee has not extensively delved into the detail of taxation law, which is vast and beyond the capacity of the Committee's resources in the period of inquiry. Rather, the Committee has explored the broader taxation eco-system, both domestic and global, the factors influencing that environment, and the way stakeholders perceive and operate within it. Importantly, the Committee has considered what influences positive taxpayer behaviour in their interaction with the tax system and what constitutes favourable engagement frameworks.
- 1.5 The Committee considered new payment platforms, use of Information Technology (IT), cyber-currencies and the potential use of blockchain technology for administrators and regulators. And against that backdrop, and that of the Government's 'digital by default' agenda, the role of cyber-resilience, cyber-security and access to the tax system for all stakeholders; not just the digitally astute or the affluent.

Explanatory paper

- 1.6 There was limited specific comment during the inquiry on tax regulation per se.⁴ This response aligned with the principal intent of the inquiry as revealed

³ *Australia's Future Tax System (AFTS) Review, Final Report*, 2 May 2010, often referred to as the 'Henry Tax Review' due to the Chairmanship of the panel by Dr Ken Henry AC.

⁴ The Goods and Services Tax (GST) and Capital Gains Tax (CGT) were discussed in some detail in select submissions.

in the explanatory (or background) paper provided by the Treasury to provide guidance on the reference. The explanatory paper is reproduced in this report following the full terms of reference. The paper refers to the AFTS final report which imagined a 21st century tax system which would ‘allow taxpayers to engage with it in ways that meet their needs and preferences’.⁵ During the inquiry the Committee received evidence to consider whether the current tax system—in an environment not envisaged a mere eight years ago when the Henry tax review reported—is doing that, or heading in that direction.

- 1.7 The explanatory paper specifically highlights exploring overseas tax agency experiences and the use of behavioural insights⁶ in how taxpayers currently engage, how they may engage in the future and how this information could inform the longer term tax policy agenda. It was from that stance that the Committee explored not only the existing taxation environment (altered since the AFTS review due in part to rapidly evolving working practices) but also the potential (and not necessarily distant) environment, including emerging technological opportunities and potential threats.

Terms of reference—included taxpayer disengagement

- 1.8 The terms of reference for the inquiry were principally about how taxpayers engage with the taxation system (be that overtly or indirectly) but the Committee was also tasked with considering the explicit decision by taxpayers to not engage with, or not fully engage with, the tax system through ‘cash economy’ or ‘hidden economy’ means. A fortnight after the Committee’s adoption of the inquiry, on 14 December 2016, the Government announced the Black Economy Taskforce, chaired by Mr Michael Andrew AO, Chair of the Board of Taxation. The Taskforce’s work covered a broader remit than undeclared cash income—also covering illicit trade and employer fraud, amongst other areas.⁷ An interim report was released on 9 May 2017.

⁵ *AFTS Review—Report to the Treasurer*, December 2009 (May 2010), see discussion in Chapter 4.

⁶ Behavioural insights involve using a mix of traditional economic strategies with insights from psychology, cognitive science and other social sciences to determine the many ‘irrational’ factors that influence decision making.

⁷ The ‘Black Economy’ was defined in the Minister for Revenue and Financial Services 14 December 2016 Media Release by the Hon Kelly O’Dwyer MP as: ‘people who operate entirely outside the tax system or who are known to tax authorities but deliberately misreport their tax (and superannuation) obligations. The black economy can also include those engaged in organised crime, including those who engage in the production and sale of prohibited goods.’

- 1.9 The final report was released after the Federal Budget on 8 May 2018 which announced initiatives recommended in the report for near-term action.⁸ The report provides greater insights into the cash economy and how government agencies may help to tackle it.
- 1.10 The Committee's focus in the inquiry has been on cash transaction tax avoidance in legal trade, that is, the non-declaration of some or all cash income in the course of earning income—and how this may be deterred. There is, however, discussion of the nexus between this tax avoidance and illegal activity as set out in the evidence.

Inquiry process

- 1.11 The inquiry was advertised by media release, social media, the Committee and Parliament House websites and through Committee Members. The Committee sought submissions from relevant Australian Government and State Government departments and agencies, peak associations in the tax and superannuation and business sectors, regulatory bodies, academia, consultants, the emerging financial intermediary sector and social and community support organisations. Some of those contacted took up the opportunity to make a written submission to the inquiry while others participated in public hearings.
- 1.12 The Committee received 31 submissions (26 primary submissions and five supplementary submissions) to the inquiry, mostly regarding the engagement aspects of the inquiry—fewer addressed the cash economy and in some cases noted that a separate submission had been prepared for the independent Black Economy Taskforce.⁹ The submissions to the inquiry, with the exception of one submission with contents withheld, are available on the Committee's website and the full list is available in Appendix A of the report.
- 1.13 The Committee held 13 public hearings in Canberra, Sydney and Melbourne. Transcripts of these hearings are available on the Committee's website and a full list of public hearings and participants is available in Appendix C of the report.

⁸ *Black Economy Taskforce Final Report*—October 2017 (May 2018), The Treasury, see <http://treasury.gov.au/review/black-economy-taskforce/final-report/> viewed 14 May 2018.

⁹ Black Economy Taskforce submissions were not publicly available (current at 14 May 2018).

- 1.14 The Committee would like to thank all participants for their thoughtful consideration of the issues. The Committee acknowledges the important contribution to the inquiry by individuals who prepared written submissions and those who committed to attending hearings—and to the valuable contribution by tax professionals, businesses, peak associations/unions and academics who attended hearings and/or made written submissions.
- 1.15 The Committee also formally recognises the particular co-operation and appearances of the Commissioner of Taxation and his staff in preparing submissions and responses to questions on notice and appearing for hearings; and that of the Inspector-General of Taxation (IGT), his Deputy and staff in examining the details of the terms of reference both in writing and at hearings. The Committee has found the past review work undertaken by the IGT most valuable and also his current work in the review of the future of the tax profession, which at the time of writing is yet to be reported on.¹⁰

Stakeholder participation

- 1.16 Fewer individual taxpayers have participated in the inquiry relative to organisations, government agencies and academics—however, academics and individuals representing organisations including tax professionals and businesses have commented on personal experiences and those of members, clients or family.¹¹ This mix is unsurprising given the Australian cultural context.¹² The subject matter is likely to reduce the gathering of primary evidence from the Australian ‘in the street’—taxation generally being accepted as a necessary impost and a subject area requiring expertise. The

¹⁰ See <igt.gov.au/publications/reports-of-reviews/review-into-the-future-of-the-tax-profession/> viewed 6 March 2018.

¹¹ Members of the Committee have also commented about constituent concerns from their electorates.

¹² The former Department of Immigration and Border Protection (2016) publication ‘Life in Australia—Australian Values and Principles’ provides an overview of ‘Australian values’ which include, amongst others, a ‘commitment to the rule of law’, a ‘spirit of egalitarianism that embraces mutual respect, tolerance, fair play’ and, ‘the pursuit of the public good’. The publication does not however mention any cultural norms regarding paying tax on income earned. <www.homeaffairs.gov.au/LifeinAustralia/Documents/lia_english_full.pdf> viewed 7 February 2018.

history of the Committee also shows lower levels of general public comment than social policy subject matter committees.¹³

Context of inquiry subject matter

- 1.17 The remainder of this chapter provides an overview of the vision and recommended facets of a well-functioning tax system as envisaged in the Australia's Future Tax System review (AFTS) report, in particular regarding the client experience of the tax and transfer system. This report stated that a modern tax system required 'citizen-centric design'.¹⁴ Although this report went into tax regulation detail at both federal and state/territory levels, beyond the scope of this inquiry, it does provide an important context for the tax environment (which is largely still the same framework) that stakeholders are operating in and engaging (or disengaging) with. The report was specifically referred to in the explanatory paper to the terms of reference to this inquiry and it provides context for discussion in other chapters of this report.
- 1.18 Following the AFTS overview this chapter outlines the *Reinventing the Australian Taxation Office (ATO) Program* which was announced in a 'blueprint document' in 2015 as the forward-looking direction of the Australian tax administrator. Its key focus was on repositioning the ATO as 'a contemporary, service-oriented organisation'.¹⁵
- 1.19 The other chapters in the report broadly cover the following areas:
- Chapter 2 discusses modern taxation administration and relevant contemporary developments overseas;
 - Chapter 3 details the tax engagement points (or cycle) for the main stakeholders and the way in which they engage or are expected to engage with the tax system;
 - Chapter 4 considers the mechanisms the ATO uses for outreach, education and the facilities it provides or intermediates for stakeholders

¹³ For example, in all inquiries undertaken by the Committee since its establishment, the highest input by individuals was to the Tax Disputes inquiry—around half the submissions—however, all but a few of these submissions were not from legal or accounting professionals.

www.aph.gov.au/Parliamentary_Business/Committees/House/Tax_and_Revenue/Inquiry_into_Tax_Disputes/Submissions> viewed 7 February 2018.

¹⁴ AFTS, Vol. 2, G4. 'Client Experience of the Tax and Transfer System', p. 697.

¹⁵ ATO, *Program Blueprint—Reinventing the ATO*, March 2015, p. 1.

to engage with the tax and superannuation system (covering behavioural insights and compliance costs in these dealings);

- Chapter 5 discusses the nature and prevalence of cash economy tax evasion, its nexus with criminal activity, the potential impact of digital payment systems and currency, and considers possible measures to reduce cash-based activity.
- Chapter 6 concludes with the key challenges of the current and emerging tax framework for taxpayer engagement—essentially being the willing and unimpeded participation of taxpayers—and any potential solutions (or future-proofing preparations) required.

Australia's Future Tax System review findings—2010

1.20 The vision of Australia's future tax (and transfer) system for the first half of the century was described in the executive summary of the *AFTS Review Report to the Treasurer*, December 2009.¹⁶ The tax system was envisaged to be efficient, equitable, transparent and effective and would need to support 'per capita income growth rates at the upper end of developed country experience'.¹⁷ It would do this through high workforce participation, efficient savings and investment in education and infrastructure. It was also envisaged to encompass the following characteristics:

Through both its direct and indirect effects, it would support the commitment to Australian values of fairness, and support for those who are disadvantaged. It would exploit opportunities to reduce compliance costs and make interactions with the tax and transfer system easier, more certain, and more understandable. It would enhance the accountability of governments to their citizens.¹⁸

1.21 The architecture of a best-case tax system for Australia was proposed in the review and the main proposals were outlined under nine broad themes. The

¹⁶ This review was commissioned by the Rudd Labor Government in 2008, and undertaken over 18 months by a panel comprising two federal government departmental secretaries, two academics and the head of a peak Australian industry association—supported by a multi-departmental working group and a secretariat provided by Treasury. It was bounded by a direction to reflect the then government's policy of not increasing or broadening the GST base and to preserve tax-free superannuation payments for the over 60s. See *AFTS*, December 2009, Part One, Overview, p. xvii.

¹⁷ *AFTS Review*, December 2009, Part One, Overview, p. xvii.

¹⁸ *AFTS Review*, December 2009, Part One, Overview, p. xvii.

report collectively made 138 specific recommendations under the following key areas—

- 1 Revenue raising through four efficient tax bases:
 - a. personal income;
 - b. business income;
 - c. private consumption; and
 - d. economic rents from natural resources and land.
 - 2 Configuring taxes and transfers to support productivity, participation and growth.¹⁹
 - 3 An equitable, transparent and simplified personal income tax.²⁰
 - 4 A fair, adequate, and work supportive transfer system.
 - 5 Integrating consumption tax compliance with business systems.²¹
 - 6 Efficient land and resource taxation.
 - 7 Completing retirement income reform and securing aged care.
 - 8 Toward more affordable housing.²²
 - 9 A more open, understandable and responsive tax system.
- 1.22 While several of the preceding nine areas are beyond the scope of this inquiry, the Committee did receive comment in many of them. On a high level, it is difficult to examine taxpayer engagement without the context of the taxation regime within which it occurs. Themes in category one, ‘revenue raising on four efficient tax bases’, which highlight the tax engagement entities and engagement points—and in category nine, which

¹⁹ Tax theory and research suggest that the structure of taxes has a major impact on workforce participation and productivity and thus long-term economic prosperity.

²⁰ That personal tax compliance had become ‘inordinately complex and complexity hides its policy intent from citizens’. It suggested a much higher tax-free threshold of \$25 000, two tax brackets and simplified superannuation, work-related deductions and offsets. In 2011–12 the tax free threshold jumped from \$6 000 to \$18 200, where it remains today.

²¹ The report stated that the GST was designed using ‘tax invoice standards more suited to the documentary standards of the 1960s than the digital potential of the 21st century’. *AFTS*, December 2009, Part One, Overview, p. xxi.

²² Recommended increasing rent assistance, a phased move to a uniform land tax and no stamp duties and to a neutral treatment of rental and owner-occupied housing.

stipulates that citizens should have access to a more transparent and understandable system (and more effective mechanisms to engage)—hold the most applicability to this inquiry.

- 1.23 Category nine is about being ‘citizen-centric’ and highlights, significantly, how critical the maintenance of the *integrity* of the tax system is and that ‘threats be promptly dealt with as they emerge’.²³ More will be discussed on this in Chapter 3. Chapters 5 and 6 of this report consider threats identified in this inquiry which may have non-trivial impacts on the stability of the tax system, impede its operation and reduce stakeholder confidence in engaging. Chapter 5 focuses on the cash economy in particular.
- 1.24 Some aspects of the AFTS review report theme three—‘an equitable, transparent and simplified personal income tax system’—have also been raised during the inquiry, including rationalising deductions and offsets.²⁴ The Committee was therefore unsurprised to receive commentary in evidence that taxpayer engagement occurs within a complex and often daunting tax and superannuation environment and that compliance costs for the taxpayer can be high.
- 1.25 There has been very little change to the overall framework of Australia’s tax and superannuation system since the AFTS review was started a decade ago but there have been myriad of changes within the system. For example, the superannuation system experienced no less than 16 regulatory changes effective as of 1 July 2017.²⁵
- 1.26 The head of the AFTS panel, Dr Ken Henry AC (current Chairman of National Australia Bank) recently reflected on tax reform progress since the review.²⁶ He said:

²³ *AFTS Review*, December 2009, Part One, Overview, p. xxiv.

²⁴ In particular, the treatment of work-related deductions was explored, which has been the subject of a recent House Standing Committee on Economics inquiry—see *Report on the Inquiry into Tax Deductibility*, June 2017, Canberra.

²⁵ Refer ATO, *Guidance Notes for Super Changes*, see <<https://www.ato.gov.au/Individuals/Super/In-detail/Guidance-notes-for-super-changes/>> viewed 14 May 2018.

²⁶ Dr Ken Henry AC, Chairman of National Australia Bank, address to the Australian Institute of Company Directors (AICD) Governance Summit, Melbourne, 2 March 2018. <news.nab.com.au/nab-chairman-dr-ken-henry-ac-speech-to-the-aicd-governance-summit/> viewed 3 March 2018.

Australia's economy is fundamentally in a good place with strong jobs growth and near-record high business conditions, likely to be supportive of strong business investment. We have a lot going for us, but not everything.²⁷

- 1.27 He highlighted two changes to Australia's business environment since 2008—which cause significant impact on the tax system—dramatic changes to the labour market including rising part-time and casual work and employment status changes, along with transformational technological development disruptions. In addition, he highlighted the fastest growing population in the developed world, along with an ageing population. The Committee has explored, in particular, the impact of the first two challenges on the tax system—labour and technology change, and they will be discussed in Chapter 6. The demographic changes further affect various areas of taxation policy and engagement.

Reinventing the ATO Program Blueprint summary

- 1.28 In 2015 the ATO announced it had implemented a broad program of change or 'reinvention' which it laid out in a program blueprint following initial consultation and co-design with stakeholders. This was partly precipitated by the Australian Public Service Commission's capability review in 2013 which tasked the ATO with transforming 'its existing processes, systems, culture and its highly capable workforce to be more agile, responsive, efficient and effective'.²⁸ The reinvention program was designed to better meet '...the needs and expectations of the community, while delivering on our commitments to government and the community'.²⁹
- 1.29 The Commissioner of Taxation, Mr Chris Jordan AO promised to transform the way in which ATO clients experienced the tax system:

We will be unwavering in our focus on improving the client experience, and will constantly check to ensure we are providing contemporary service that is conducive to willing participation in the tax and super systems.³⁰

²⁷ Dr Henry AC, address to the AICD Governance Summit, Melbourne, 2 March 2018.

²⁸ Australian Public Service Commission, *Capability Review: Australian Taxation Office*, May 2013, p. 6. This review focused on leadership, strategy and delivery capabilities in the ATO.

²⁹ These included productivity, efficiency and deregulation.

³⁰ ATO, *Program Blueprint—Reinventing the ATO*, March 2015, p. 1.

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- 1.30 The program considered how to emphasise a culture of integrity and driving cultural change to align with the new, more technologically focused client experience in the tax and superannuation systems. The new client experience was being driven by a changing business and working environment and the changing expectations and capabilities of Australian taxpayers—along with meeting efficiency gains in the ATO.
- 1.31 The program comprised:
- behavioural and cultural elements;
 - locally managed change and application of continuous improvement; and
 - six strategic programs overseeing 100 projects.³¹
- 1.32 The APSC’s capability review summed up the important and varied role of the Australian tax administration agency, noting it was not purely a collector of revenue, but also involved in social policy and transfer payment programs:
- The ATO is the government’s principal revenue collection agency and administers a wide range of tax legislation. It has an important role in various other economic and social policies as a large payer of government funds, administrator of major elements of the superannuation system, custodian of the Australian Business Register and provider of valuation services through the Australian Valuation Office. The work of the ATO touches the lives of all Australians. Revenue collected supports most publically funded services and plays a vital role in ensuring Australia’s prosperity.³²
- 1.33 The Australian National Audit Office (ANAO) has recently tabled a performance audit report of the costs, savings and benefits of the Reinventing the ATO Program³³, approximately 2.5 years after the program commenced. The ATO was found to have been unable to measure and monitor the total costs of implementing the 100 reinventing the ATO projects due to low levels of staff conformance with internal cost tracking

³¹Appendix 2, Australian National Audit Office (ANAO), ‘Costs and Benefits of the Reinventing the ATO Program’, *ANAO Report No. 15 2017–18*, November 2017.

³² Australian Public Service Commission (APSC), *Capability Review: Australian Taxation Office*, May 2013, p. 2.

³³ ANAO, ‘Costs and Benefits of the Reinventing the ATO Program’, *ANAO Report No. 15 2017–18* November 2017.

requirements.³⁴ The collective costs of 67 of the 100 projects which had available data were estimated to be \$300 million from 2013-14 to 2018-19. Monetary savings had not been tracked but as at April 2017 internal reporting on financial benefits were introduced across the office, including on these 100 projects.

- 1.34 It is important to note, however, that tangible outcomes of the 100 projects were identifiable and the ATO's response to the ANAO findings clarified that most of the reinventing of the ATO program was in cultural change and localised action rather than through explicit programs. The purpose of the reinvention program was to transform the agency to provide 'a stronger connection to the community and an openness and willingness to change in order to maximise willing participation in the tax and superannuation systems'.³⁵ Through a connected benefits management system that links projects and program outcomes the ANAO determined that there was indeed a general improvement across the ATO's corporate benefit categories of integrity, willing participation, revenue and productivity from 2013-14 to 2015-16 (merely two periods), particularly in the areas of willing participation and revenue.³⁶
- 1.35 Within the integrity category the Committee noted that community satisfaction with ATO performance had actually deteriorated between 2013-14 and 2015-16. This may merely reflect the views of those seeking a particular performance outcome/decision by the ATO rather than those enjoying the 'improved client experience' as reported under the much improved category of willing participation.
- 1.36 Notwithstanding this, given the tendency of the ANAO's review finding, the Committee's overall impression is that the Reinvention program has failed to achieve its agreed outcomes. The serious service outages over December 2016 and February 2017 and the ATO's failure to recognise or chart ongoing problems — with the technical criterion for a breach being over four hours of outage, suggests that the ATO's performance could look much worse.

³⁴ ANAO 'Costs and Benefits of the Reinventing the ATO Program', ANAO Report No. 15 2017-18: November 2017, p. 9.

³⁵ ANAO, 'Costs and Benefits of the Reinventing the ATO Program', ANAO Report No. 15 2017-18: November 2017, p. 10.

³⁶ The ATO uses measurement methods which include surveys. Details of performance appear in the ATO, *Commissioner of Taxation Annual Report 2016-17*, October 2017.

- 1.37 The Committee notes that willing participation is clearly a key measure of success in taxpayer engagement. Willing participation will reflect the percentage of taxation collected which tax regulation allows. The quantum of tax collected, on the other hand, reflects the underlying structure of the tax system, the buoyancy of the economy and whether it is efficient, effective and fair.
- 1.38 As the AFTS review highlighted in its final report, simplicity in the tax system is not costless and that there are winners and losers in tax reform in the short to medium term. This, and the certainty of the tax and superannuation system framework, impacts taxpayer 'buy-in' – and ultimately affects their engagement or 'willing participation'.

2. Modern tax systems

Introduction

- 2.1 This chapter provides an overview of current practice in tax administration in some comparable countries. It considers general trends and the new ethos underpinning the transformation in tax services in response to technological change. The chapter serves as a background for the comparison and evaluation of the Australian Taxation Office (ATO)'s services and functions which is a subject of this report.
- 2.2 The inquiry terms of reference invited examination of tax administration processes and services within comparable countries in areas of communication and information technology, and in compliance activity. The broader context for this was to consider how voluntary compliance could be motivated through the use of behavioural insights, information technology, automated and natural systems, and 'nudges'.¹ An additional focus was on emerging enforcement challenges, in particular for mechanisms to reduce and disrupt the cash economy.
- 2.3 During the inquiry, there was discussion of the implementation of digital automated systems and processes in Sweden, the United Kingdom and New Zealand in particular. Consideration was given as to how digitisation is

¹ A 'nudge' is a concept in behavioural science, political theory and economics which proposes positive reinforcement and indirect suggestions to try to achieve non-forced compliance to influence the motives, incentives and decision making of groups and individuals.

transforming taxpayer engagement, supporting innovation in tax administration and regulatory reform.

- 2.4 Compliance and enforcement responses to the cash and shadow economies in different jurisdictions were raised in the latter context. A brief overview of these, along with the challenges associated with the emergent ‘gig’ and sharing economies, conclude the chapter. The cash economy is discussed in more detail in Chapter 5.
- 2.5 Information in this chapter is supplemented by analysis in the Organisation for Economic Co-operation and Development (OECD)’s *Tax Administration 2017* report, which provides internationally comparative data on trends in 55 advanced and emerging economies.²

Tax administration processes and services

- 2.6 In narrow terms, tax administration refers to the rules and processes for collecting and disbursing revenue and payments administered by a nations’ revenue authority.³
- 2.7 The OECD’s 2017 comparative review found significant change had taken place in tax administration over the survey period, being driven by:
- (i) the use of new technologies, tools and data to improve the effectiveness and delivery of contemporary services;
 - (ii) the desire to reduce the cost of tax operations and burdens on taxpayers;
 - (iii) the taking on of new responsibilities; and

² The Organisation for Economic Co-operation and Development (OECD) Centre for Tax Policy and Administration produces a biennial review of tax administration as part of its Tax Administration Comparative Information Series. The review reports provide internationally comparative data up to the end of the 2015 fiscal year. See Forward, OECD, *Tax Administration 2017 Comparative Information on OECD and Other Advanced and Emerging Economies*, 29 September 2017 (hereafter OECD, *Tax Administration 2017*) <www.oecd.org/ctp/administration/tax-administration-23077727.htm> viewed 20 December 2017.

³ New Zealand Government, *Making Tax Simpler—Towards a New Tax Administration Act—a Government Discussion Document*, The Hon. Todd Mackey, Minister of Revenue, November 2015, p. 6.

(iv) the implementation of the far-reaching and major changes to the international tax rules, including the outcomes under the OECD/G20 Base Erosion and Profit Shifting (BEPS) Project.⁴

2.8 The Chair of the OECD's Forum on Tax Administration Edward Troup advised in his preface to the report:

Tax administrations are embarking on a period of unprecedented change. The emergence of new technologies, analytical tools and a vast increase in the scope and scale of digital data offer significant opportunities to enhance tax administration and reduce burdens. But there are also challenges to realising these benefits. These include pressures on budgets and human resources, the capacity of tax administrations to respond swiftly to rapid changes in business models and the choice of cost-effective technical solutions.⁵

2.9 Evidence to the Committee suggests that the combination of technological change, globalisation and budgetary pressure has already transformed global tax administration practice. Mr Richard Highfield, a former Australian Taxation Second Commissioner and current Adjunct Professor at the University of New South Wales School of Business, observed:

Modern tax systems and their administration are built on the principle of "voluntary compliance" – taxpayers are expected to comply voluntarily with their tax obligations with only limited intervention by tax officials. In practice, voluntary compliance is achieved through what are termed "self-assessment" procedures. Under self-assessment, taxpayers are expected to calculate their own liabilities, submit their own returns and payments, and provide further information when requested.⁶

2.10 The expectation that taxpayers should 'self-assess' their tax status has ushered in a need for revenue agencies to simplify processes and educate the community about their tax obligations, as well as that revenue agencies improve risk analysis and monitoring processes. Mr Highfield commented:

To encourage high levels of voluntary compliance, the conventional wisdom is that tax bodies should provide an extensive array of education and assistance-related products and services to help taxpayers meet their obligations with minimal burden and costs. Tax bodies also conduct risk-based programs of

⁴ Executive Summary, OECD, *Tax Administration 2017*, p. 17.

⁵ Preface, OECD, *Tax Administration 2017*, p. [6.]

⁶ Mr Richard Highfield was the Second Commissioner of Taxation from 1991 to 1997. See *Submission 6*, pp. 2, 3.

verification and enforcement to detect and deter non-compliance. The tax laws also provide for the imposition of sanctions (e.g. penalties and interest) to encourage voluntary compliance and to punish those who are found to have not complied.⁷

The wider tax eco-system

- 2.11 In response to the new taxation environment, taxation agencies are now looking more holistically at the problem of tax engagement. This includes engagement with domestic and global partners to address emerging compliance challenges.
- 2.12 ATO Deputy Commissioner, Digital Delivery, Mr John Dardo referred to the concept of a 'tax eco-system' in discussion of domestic tax security – incorporating tax agents, BAS (Business Activity Statements), software developers and super funds.⁸ The OECD 2017 report also used this term, confirming that tax administration now goes beyond management of 'effective and efficient internal systems' to 'the stewarding of the wider tax eco-system', which includes the private and public sector, and international partners.⁹ The report explained:

In concrete terms this means [tax administrators] are looking at how they can deploy new technologies and new delivery approaches to improve their effectiveness as well as the efficiency of their operations. In addition they are engaging with third party providers of data and services in new business arrangements that extend the traditional view of the tax eco-system, including through monitoring and standard setting. To compound the challenges, these changes are taking place at the same time that administrations are implementing major changes to the international tax rules, responding to the tax issues surrounding new economic systems (including the digital and sharing economies) and taking measure to further reduce the tax gap.¹⁰

- 2.13 Stewardship of this extended tax eco-system also means modern tax administrators have responsibilities beyond traditional enforcement activities in a new governance model which involves: 'lowering costs,

⁷ Mr Richard Highfield, *Submission 6*, p. 3.

⁸ Mr John Dardo, Deputy Commissioner, Digital Delivery and Chief Digital Officer, Australian Taxation Office (ATO), *Committee Hansard*, Canberra, 27 October 2017, p. 23.

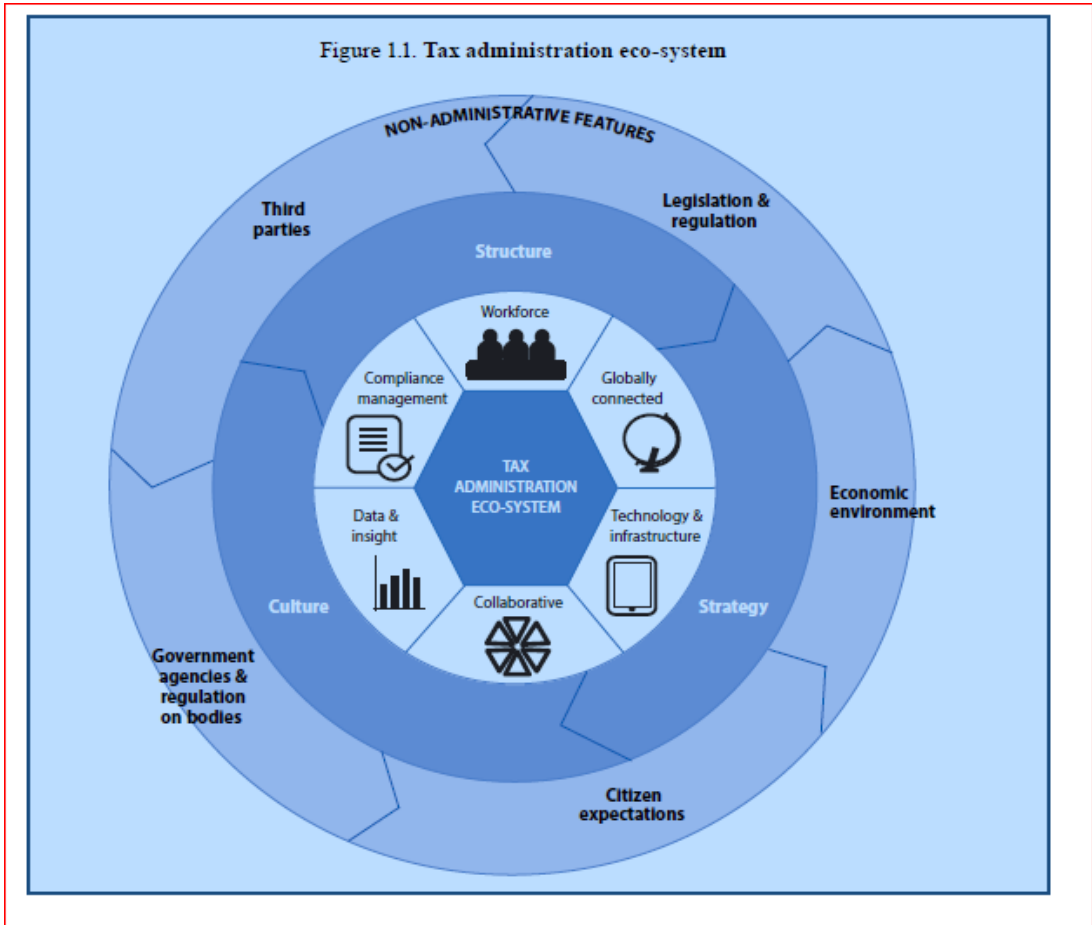
⁹ OECD, *Tax Administration 2017*, p. 29.

¹⁰ OECD, *Tax Administration 2017*, pp. 28–29.

enhancing voluntary compliance and reducing the burdens arising from paying taxes, thus helping to promote growth and investment'.¹¹

2.14 A figure showing the model for tax administration under this broader mandate follows.

Figure 2.1 The tax administration eco-system



Source: OECD, *Tax Administration 2017*, p. 28.

¹¹ OECD, *Tax Administration 2017*, p. 28.

The digital revolution in tax services

- 2.16 The progressive digitisation of taxation services is a feature of the integrated tax eco-system set out above, and hence a policy and investment priority for most advanced nations.¹²
- 2.17 Rather than being internally generated by governments, the phenomenon is couched as a necessary response by tax administrators to the penetration of digital services and systems across the modern taxpayer base. The OECD observes:
- An increasingly digital, mobile and global taxpayer base is requiring tax administrations to respond to issues that were once only the domain of its largest businesses. These changes are prompting administrations to consider how they can best support this growing group of taxpayers. In particular they are looking at how they can provide easier approaches to compliance, including embedding tax requirements in the processes and applications that taxpayers use on a day to day basis, providing greater tax certainty and reducing costs.¹³
- 2.18 As noted previously, the discussion of the digital transformation of tax services is linked with the associated need to promote ‘voluntary compliance’. Hence the importance of seamless engagement with customer preferred ‘natural systems’, those used in the community to run businesses, manage bank accounts, or to interact with government services such as education, health and welfare.¹⁴
- 2.19 The ATO’s digital strategy responds to this need committing to:
- Streamline and embed our services into the systems our clients use everyday

¹² See for example, *ATO Digital Strategy*, December 2016, Appendix 2, *ATO Submission 15*, Her Majesty’s Revenue and Customs (HMRC, United Kingdom,) *Making Tax Digital, Policy Paper*, December 2015, updated July 2017, <www.gov.uk/government/publications/making-tax-digital> Inland Revenue Department (IRD, New Zealand) *Tax Policy*, Chapter 6: A Better Customer Experience using Digital Services, <taxpolicy.ird.govt.nz/publications/2015-dd-mts-2-better-digital-services/chapter-6> viewed 20 December 2017.

¹³ OECD, *Tax Administration 2017*, p. 29.

¹⁴ See ‘Technologically Enabled’, OECD, *Tax Administration 2017*, p. 29, and see ATO *Blue Print for Change*, Program Summary, ATO Reinvention Program <www.ato.gov.au/About-ATO/About-us/Reinventing-the-ATO/Program-blueprint-summary/> viewed 19 December 2017, and discussion Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, pp. 22–23.

- Facilitate seamless transactions between individuals, government, and businesses by embedding our services within the systems our clients use day-to-day (eg software, banking, point of sale)
- Streamline and automate reporting obligations, integrating the collection of data and making it easier for clients to complete reporting obligations (eg payroll events)
- Explore opportunities to leverage from new and emerging technologies
- Work with third parties to improve access, frequency and integrity of data sources.¹⁵

2.20 An additional benefit of the automation of tax, government and financial systems is the potential to more efficiently collate and crosscheck information received. The OECD suggests that lower storage costs coupled with advances in data analytics technologies have allowed tax administrators to not only source more third-party data, including through development of new methods and products, but has also enabled better management of tax risks.¹⁶

2.21 Automated pre-filling of tax information, payment registration and e-invoicing systems, along with the introduction of perceptive assessment tools which select and predict taxpayer responses, have been variously adopted by comparable tax revenue agencies. Sweden has led the transition to real-time sales and tax inputs by mandating use of certified point of sale systems, and by popularising the use of mobile apps to promote community acceptance that tax compliance is the norm.¹⁷

2.22 These mechanisms are also seen to offer opportunities to make more fundamental reforms to the structure and operation of tax systems. Pre-filling, for example, can suspend the need for taxpayers to make periodic lodgement of tax material, allowing for tick box or no return systems for a majority of taxpayers, as in New Zealand. A more immediate real-time tax registration process, using point of sale technologies, can allow taxpayers to look at tax owed in advance rather than find out how things stand later after a return or Business Activity Statement has been processed.

¹⁵ 'Priority Themes', *ATO Digital Strategy*, December 2016, p. 9, Appendix 2, ATO, *Submission 15*.

¹⁶ OECD, *Tax Administration 2017*, p. 19.

¹⁷ See Board of Taxation, *Submission 17*, 'Annexure A – The Overseas Experience' (Appendix D in these pages at p. 191) and see Annex 3, J Henly, 'Sweden leads the Race to become the Cashless Economy', *The Guardian*, 5 June 2016 in Richard Highfield, *Submission 6*, p. 26.

- 2.23 The following section provides a snapshot of engagement technologies in comparable nations.

Self-service and pre-filing of tax information

- 2.24 In its overview of trends in tax administration, the 2017 OECD tax administration report observed that although the shift to digital services over the last two decades was at first slow, now most tax administrators offer taxpayers web-based services providing the ability to register, file and pay online. Two thirds of tax administrations also offered taxpayers an integrated online account.¹⁸
- 2.25 However, the 2017 study also revealed that, despite these advances, online lodgement for individuals has lagged behind. While electronic lodgement was high for business (four out of five for corporate and Value Added Tax – VAT) only two out of three individual taxpayers lodged online.¹⁹
- 2.26 Tax administrators anticipate that achieving higher usage of electronic lodgement and payment systems will both reduce costs and improve services to taxpayers.²⁰ One of the more significant innovations in this regard over the last two decades has been provision of pre-filled tax information for individual tax payers.²¹
- 2.27 The ATO's submission to the current inquiry sets out recent outcomes resulting from improved delivery of pre-filled information:

Since the introduction of myTax it is estimated that it has delivered a reduction in the cost of compliance for individual taxpayers of approximately \$285 million per year.

As at April 2017, over 3.2 million 2015–2016 individual income tax returns have been lodged using myTax. It is available on any device, at any time convenient to the taxpayer.

The return on investment for the Australian Tax Office arises from the fact that taxpayers are more likely to voluntarily comply with their obligations when doing so is quick and easy. Taxpayers using myTax also have access to a pre-

¹⁸ OECD, *Tax Administration 2017*, p. 92.

¹⁹ OECD, *Tax Administration 2017*, p. 82.

²⁰ OECD, *Tax Administration 2017*, p. 81.

²¹ OECD, *Tax Administration 2017*, p. 82.

filling service that makes it easy to ensure they have not omitted income such as salary and wages or dividends and interest.²²

2.28 The Inspector-General of Taxation referred to the results of the 2015 OECD tax review which found that almost half of the revenue bodies surveyed at the time made use of pre-filing.²³ Scandinavian countries provided full pre-filing, with many taxpayers needing only to accept the information rather than lodge their own returns. The submission noted:

Denmark was the first Scandinavian country to introduce pre-filled tax returns in the 1990s, followed by Sweden and Norway. In Sweden, taxpayers can accept a pre-filled return by internet, phone, SMS or paper. Since 2009, Norway has adopted a silent acceptance approach whereby if taxpayers do not respond to the pre-filled income tax return, it is treated as final and binding. Similarly, in Denmark a 'no response' is deemed to be acceptance of the return. The OECD has reported that, the Scandinavian countries experienced a 50 to 75 percent rate of returns not requiring adjustment by taxpayers.²⁴

2.29 The most recent OECD tax administration study highlighted further developments. Nine jurisdictions—Estonia, Finland, Iceland, Lithuania, Norway, Peru, Portugal, South Africa and Sweden, now provide almost full coverage of pre-filled information for personal tax payers. The pre-fill regime adopted by 11 jurisdictions further extended the services to provide a 'deemed acceptance' after a predetermined expiry period.²⁵

2.30 The OECD review anticipated that improved data flows from third party data providers, along with changes to the design of tax administration systems, could allow more tax administrators 'to verify returns immediately, or to pre-fill tax returns or, eventually, to dispense with them altogether'.²⁶

2.31 In his submission, Mr Highfield advised the Committee of recent developments in this direction in the United Kingdom:

Over the last two years, Her Majesty's Revenue and Customs has implemented a process whereby employee taxpayers who are not required to prepare and file a tax return now receive a personal tax summary from HMRC

²² ATO, *Submission 15.1*, p. 4.

²³ OECD, *Tax Administration 2015, Comparative Information on OECD and other Advanced and Emerging Economies*, 2015, p. 267.

²⁴ OECD, *Tax Administration 2015*, cited in Inspector-General of Taxation (IGT), *Submission 5*, p. 24.

²⁵ OECD, *Tax Administration 2017*, p. 83.

²⁶ OECD, *Tax Administration 2017*, p. 18.

during the following year. The statement draws on third party information acquired by HMRC and seeks to formalise taxpayers' engagement with the tax system and to improve the transparency of the UK personal tax system.²⁷

- 2.32 The Committee noted that the jurisdictions referred to in this section have significantly less complex tax systems, better lending themselves to the cited innovations. The significance of tax complexity in the Australian context is discussed further in the body of this report.

End-to-end solutions

- 2.33 As shown on *Figure 2. 1* in this chapter, the modern tax administration ecosystem comprises many partners in the public and private sectors, as well as the taxpayers themselves. This, as the OECD has observed, has prompted tax administrators 'to design integrated services that extend beyond the tax system itself'.²⁸
- 2.34 Australia's Single Touch Payroll and SuperStream services are examples of systems which deliver these 'end-to-end solutions' — those that integrate with the 'natural systems', such as payroll and accounting products, used by taxpayers.²⁹ The ATO submission advised of the efficiencies that these products afford the agency and businesses:

One of the significant improvements for businesses who are employers is SuperStream, which has streamlined the process of paying superannuation contributions for employees allowing them to use a single channel to pay multiple funds. It is expected to deliver savings to employers of approximately \$350 million per annum. Single Touch Payroll will further streamline and automate reporting obligations for employers through their regular payroll events.³⁰

- 2.35 Xero Australia is a major software development partner working with the ATO on its Standard Business Reporting, online tax lodgement, SuperStream and e-invoicing services.³¹ Mr Matthew Prouse, Xero's Partner Solutions

²⁷ Mr Richard Highfield, *Submission 6*, Footnote 3, p. 4.

²⁸ OECD, *Tax Administration 2017*, p. 166.

²⁹ C O'Neill, ATO, 'Using Digital Delivery to Enhance the Integrity of Tax Systems', OECD, *Tax Administration 2017*, p. 166.

³⁰ ATO, *Submission 15*, p. 11.

³¹ Mr Matthew Prouse, Partner Solutions Manager, Xero Australia Pty Ltd, *Committee Hansard*, Canberra, 27 October 2017, p. 1.

Manager, described how his firm delivers compatible products to connect with these systems:

From a technology perspective, there is an ecosystem being built around the core accounting platforms. Xero is a global accounting platform. We provide effectively a horizontal accounting engine that integrates through to the ATO if you are a tax agent. On top of that, there is a thriving ecosystem of industry specific vertical applications. We have over 600 that integrate to our platform that were developed by over 40 000 people. There are 40 000 developers building software on top of the Xero software stack, and some of those are quite industry specific. There are third party apps developed here in Australia that do the accounting on top of Xero for agriculture, farming or wine production. There are a variety of these sorts of vertical applications. In some cases, they are bringing in not just the tax compliance calculations but some other regulatory work as well—the reporting for child care, for example, or the health care industry. There is some statutory reporting that needs to be captured and contained in software digitally as well.³²

- 2.36 E-invoicing is a registration system for electronically sending, receiving and storing invoices between suppliers and buyers, either business to business or business to government. Australia’s e-invoicing system is still in development,³³ but other jurisdictions have already mandated use of e-invoicing services. The OECD considers that the approach has potential to further modernise tax systems, supporting real-time tax assessment and enhancing compliance. For example:

Brazil is among a number of countries that have mandated e-invoicing... This has helped establish a national digital bookkeeping system, “SPED”, which enables direct reporting of annual income taxes and other tax information. The Brazilian tax administration can now review, assess and act on some information almost instantly, including issuing penalties in near real-time. As a result, the number of audits, their assessed value and total tax collected has significantly increased. There is also greater overall reported participation in the tax system.³⁴

³² Mr Prouse, Xero Australia Pty Ltd, *Committee Hansard*, Canberra, 27 October 2017, p. 4.

³³ In February 2017, the Digital Business Council announced that the first ‘end to end electronic invoicing experiment’ was being conducted with the Commonwealth Bank, Telstra and MessageXchange, see <digitalbusinesscouncil.com.au/Commbank-eInvoice> viewed 21 January 2018.

³⁴ OECD, *Tax Administration 2017*, p. 166.

2.37 Application Programming Interfaces (APIs) provide the means by which e-invoicing and the different types of electronic systems and products communicate securely.³⁵ Deputy Commissioner John Dardo suggested that the ATO's investment in APIs made Australia a leader in this area:

What I would say to you is that APIs are a metric of that digitisation. We have met with the OECD leading edge revenue agencies in a number of international forums now. We have been asked by the OECD to lead some work around how APIs are managed and regulated. As far as we know, we have not found a single country that has as many APIs as we do with as broad a range and with the sensitivity we do. In fact, if you had asked me three months ago, I think I would have said that the cumulative figure of all the APIs around all other revenue agencies was still less than what we had. So we are that far ahead.³⁶

Point of sale systems and mobile payment apps

2.38 While the trend towards electronic payments and 'tap-and-go' contactless cards in Australia is strong,³⁷ some jurisdictions overseas are more advanced in implementing fintech developments which support the shift away from cash.

2.39 As noted previously, Sweden has mandated for implementation of certified cash registers — 'the black-box' — to provide real-time information to the Swedish Taxation Authority (STA) on sales transactions.³⁸ The OECD comparative report advised of the measure's effectiveness in reducing the cash economy, and increasing revenue collection in Sweden:

Since the 1990s, several jurisdictions have implemented mandatory electronic cash registers for retail businesses, many achieving considerable revenue increases as a result. Sweden introduced the mandatory use of certified cash

³⁵ An API is a set of commands, functions, protocols, and objects that programmers can use to create software or interact with an external system, see Tech Term <techterms.com/definition/api> viewed 21 January 2018.

³⁶ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 23.

³⁷ In 2016 credit and debit cards combined were the most frequently used means of payment, with 85 per cent of Australians holding contactless 'tap and go' enabled cards. See Reserve Bank of Australia (RBA), *How Australians Pay: Evidence from the 2016 Consumer Payments Survey, Research Discussion Paper, 2017-04*, July 2017, p. 2 <www.rba.gov.au/publications/rdp/2017/pdf/rdp2017-04.pdf> viewed 24 January 2018.

³⁸ See Board of Taxation, *Submission 17, 'Annexure A, the Overseas Experience'*, (Appendix D in this report).

registers for traders in January 2010, and supports implementation by carrying out unannounced inspections, undercover purchases and customer verifications. The Swedish Tax Agency estimates that as of 2013, this approach helped increase VAT and income tax revenues by EUR 300 million per year.³⁹

- 2.40 Other economies that have recently adopted the measure include Russia and Italy. In 2017, Russia's Federal Tax Service (FTS) commenced transition to a mandatory system allowing for immediate uploading of sales data to the FTS, with a scannable code allowing taxpayers to compare the information with FTS data. Italy's Revenue Agency meanwhile initiated the optional use of electronic cash registers for VAT operators which stores data electronically and transmits it to the Revenue Agency on a daily basis.⁴⁰
- 2.41 While use of mobile apps to make payments in store is still relatively new in Australia,⁴¹ Mr Simon Edwards, Director, Government Relations, PayPal Australia told the Committee that Sweden's transition to a predominately cashless society has also provided an enormous stimulus to private sector fintech innovation and the take up of payment apps:

I draw it back to Sweden. Sweden has become probably the Western world's pin-up child of the cashless society. It dropped its use of cash down to very small numbers. In that process, the FinTec application development industry in Sweden has taken off. There are hundreds and hundreds of apps that you can use in Sweden that deal with this whole issue of paying in a non-cash environment.⁴²

- 2.42 These apps have also been credited with buoying the shift away from cash in Scandinavian countries, as they provide real-time clearance like cash transactions.⁴³ Mr Highfield provided information on the following products:

³⁹ OECD, *Tax Administration 2017*, p. 60.

⁴⁰ Box 4.4, Use of Certified Cash Registers, OECD, *Tax Administration 2017*, p. 60.

⁴¹ In an RBA survey conducted in 2016, only one percent of point of sale transactions were made using a mobile device. The RBA notes, however, that online purchases are increasingly being made by mobile phone, with around one-fifth of online retail payments made using a mobile phone in 2016, compared with 6 per cent in 2013, see RBA, *How Australians Pay: Evidence from the 2016 Consumer Payments Survey, Research Discussion Paper, 2017-04*, July 2017, pp. 12, 28, viewed 25 January 2018.

⁴² Mr Edwards, PayPal Australia, *Committee Hansard*, Canberra, 16 August 2017, p. 6.

⁴³ See Annex 3, J Henly, 'Sweden Leads the Race to become the Cashless Economy', *The Guardian*, 5 June 2016 in Richard Highfield, *Submission 6*, p. 26.

- Swish mobile app—developed jointly with major Swedish banks Nordea, Handelsbanken, SEB, Danske Bank and Swedbank, Swish is now used by 50 per cent of the Swedish population to make 900 million payments a month.
- iZettle mobile app—developed to allow small traders and small businesses to take card payments using an app and card reader plugged into the phone, which increased sales, reported up by 30 per cent.
- Denmark’s Mobilepay—had a similar take up to Swish in Sweden, with more than half the population making 90 million transactions last year.⁴⁴

Data analytics in risk management

2.43 Increasingly sophisticated data-matching capability and advanced data analytics are being deployed by tax administrators to better target compliance activities and management of risk. The OECD reports:

Tax administrations now use analytic techniques to inform a wide range of actions, including optimising debt-management processes, improving filing rates and quality, delivering better taxpayer service, and understanding the wider impact of policy changes. Moreover, many of these applications now support real-time (or near real-time) operational processes.⁴⁵

2.44 The OECD 2017 survey asked tax administrations to identify the relative priority attached to a number of risk categories in their current compliance strategies. The highest priority areas for data analysis nominated by agencies were: VAT fraud; aggressive tax avoidance schemes; the shadow economy and transactions involving zero or near zero tax jurisdictions. E-commerce, identity-fraud and high net wealth individuals (HNWIs) were medium to high priorities’.⁴⁶

2.45 Input from the Office of Revenue Commissioners Ireland advised that advanced analytics techniques are being used to ‘uncover insights from data to inform decisions and to test policies and interventions.’⁴⁷ These projects proceed on two grounds:

⁴⁴ See Annex 3 in Richard Highfield, *Submission 6*, pp. 26–27.

⁴⁵ OECD, *Tax Administration 2017*, p. 139.

⁴⁶ OECD, *Tax Administration 2017*, p. 55.

⁴⁷ OECD, *Tax Administration 2017*, p. 55.

⁴⁷ D Sinnott and R O’Carroll, Office of Revenue Commissioners Ireland, ‘Advanced Analytics’ in OECD, *Tax Administration 2017*, p. 140.

- *Predictive analytics*—which anticipates likely problems by looking for patterns in historical data; and
- *Prescriptive analytics*—which aims to uncover causal relationships, such as whether particular actions are caused by, or just coincide, with a change in taxpayer behaviour.⁴⁸

2.46 Several OECD member countries, such as Ireland, Malaysia, the Netherlands, New Zealand and Singapore, reported utilising advanced analytics to carry out social network analysis to help detect certain types of VAT fraud.⁴⁹

2.47 Other jurisdictions focussed on identifying and reducing cash economy activity. Australia and New Zealand, for example, have both utilised advanced analytics techniques to develop strategies to target high risk sectors for cash economy or tax-evasion behaviours.⁵⁰

2.48 The OECD report highlighted the role of the ATO's Nearest Neighbour model and Workplace deduction tool to showcase the utility of advanced analytics techniques in reducing fraud risks associated with work-related expenses claims:

In Australia, to support its work in managing claims for work-related expenses, the Australian Tax Office (ATO) has developed an analytical model that risk assesses taxpayer claims. In 2014–15, 8.4 million taxpayers claimed work-related expenses to the value of AUD 21.3 billion. The model, Nearest Neighbour, enables the ATO to compare a taxpayer's work-related deduction claims against those in similar jobs and earning similar amounts of income to determine how far they differ from the norm. In essence, this provides a personalised risk profile that enables the ATO to identify higher than expected claims. While a larger claim might be legitimate, it may result in the ATO clarifying the claims with the taxpayer and their employer.

In 2016, the ATO extended the use of Nearest Neighbour to operate in real-time. In myTax (the lodgement system for self-preparers), if work-related expense claims seem higher than expected, taxpayers are prompted to check their claims before submitting their returns. The ATO will introduce similar online analytics for tax agent clients for Tax Time 2017. Prompts for tax agents will alert them if a client falls outside "normal" claim parameters and may

⁴⁸ OECD, *Tax Administration 2017*, p. 140.

⁴⁹ OECD, *Advanced Analytics for Better Tax Administration: Putting Data to Work* (2016), pp 21–22, cited in IGT, *Submission 5*, p. 39.

⁵⁰ ATO *Submission 15*, p. 16.

require their further attention. The Nearest Neighbour analysis is transforming the way the ATO manages compliance, enabling greater emphasis on prevention and self-correction to encourage willing participation.⁵¹

Behavioural economics methods

2.49 Behavioural economics insight strategies use informed analysis of data, including small sample data (randomised controlled trials), to predict likely behaviours of taxpayers given particular prompts, be it in the message, communication style or method, systems design, or through other inducements or penalties.

2.50 The Chartered Accountants Australia and New Zealand (CAANZ) advised of New Zealand's recent expansion of its withholding tax regime for contractors,⁵² with the NZ Inland Revenue's report to the OECD highlighting the coinciding marketing campaign directed at tradespeople with the tag-line: 'It's just the odd under-the-table job here and there.'⁵³

2.51 The ATO has referred to work in Canada, New Zealand, Singapore, the United Kingdom and the United States of America (USA) being used to develop behavioural economics practice.⁵⁴ The submission advises:

Behavioural insights help us understand why, when and how people make decisions. From a tax administration perspective, our philosophy in applying behavioural insights is to make it as easy as possible for the community to make the right tax and superannuation decisions in ways that minimise effort and cost.⁵⁵

2.52 Professor Michael Hiscox, the Director of the Behavioural Economics Team of the Australian Government (BETA), referred to the use of pre-filling in Sweden and Estonia as behavioural economics tools:

From a behavioural point of view, it is interesting. Some of the experience internationally and, actually, in the private sector is that technology enables better service and even easier service delivery to people. We could do it

⁵¹ OECD, *Tax Administration 2017*, Box 41, 'Integrated Approach to Managing Risks', p. 56.

⁵² Mr Peter Vial, New Zealand Country Head and Tax Leader, Chartered Accountants Australia and New Zealand (CAANZ), *Committee Hansard*, Melbourne, 17 July 2017, p. 3.

⁵³ OECD, *Tax Administration 2017*, p. 61.

⁵⁴ ATO, *Submission 15*, p. 16.

⁵⁵ ATO, *Submission 15*, p. 16.

through the tax system by prepopulating more of your tax form for you, which is something that countries like Sweden and Estonia do. In Sweden, it is as simple as basically replying to an SMS to confirm that they have prepopulated everything correctly, and then you submit your taxes.⁵⁶

- 2.53 The OECD report cited Belgium's use of randomised trials to test different approaches to improve tax compliance. The project, run with Oxford University and the London School of Economics, had a trial population of 250 000 debt cases. The trails involved issuing debt letters, with different phrasing, presentation and penalty or public good messages.⁵⁷
- 2.54 Other techniques to encourage taxpayers to pay more promptly involved use of outbound phone campaigns in Canada, the United Kingdom and Norway, and reminder calls in Belgium.⁵⁸ The ATO referred to its work using text messages to prompt debt compliance and change behaviours over the 2015–2016 tax year. During the period, the Office issued 540 000 text message reminders to clients to pay on time. At tax time in 2015, the ATO deployed personalised and targeted messaging to influence the shift from etax to myTax, and from paper lodgements to online lodgements.⁵⁹
- 2.55 As noted above, several OECD member countries are using advanced analytics to carry out social network analysis to help detect certain types of VAT fraud.⁶⁰ Advanced data analysis can also assist agencies identify high risk sectors for cash economy activity, and those most prone to debt, with randomised controlled trails then used to test the most effective ways of improving compliance among targeted groups.⁶¹
- 2.56 Evidence also referred to the United Kingdom's use of extensive educational campaigns to improve taxpayer compliance, including by shifting attitudes to cash activity.⁶² The New Zealand Inland Revenue's report to the OECD

⁵⁶ Professor Hiscox, Behavioural Economics Team of the Australian Government (BETA), Department of the Prime Minister and Cabinet (PM&C), *Committee Hansard*, Canberra, 10 May 2018 p. 12.

⁵⁷ OECD, *Tax Administration 2017*, p. 56.

⁵⁸ OECD, *Tax Administration 2017*, pp. 159–60.

⁵⁹ ATO, *Submission 16*, pp. 16, 17.

⁶⁰ OECD, *Advanced Analytics for Better Tax Administration: Putting Data to Work* (2016), pp 21–22, cited in IGT *Submission 5*, p. 39.

⁶¹ OECD, *Tax Administration 2017*, p. 158.

⁶² IGT, *Submission 5*, p.8.

highlighted the marketing campaign directed at tradespeople who may receive, but not declare all cash payments.⁶³

- 2.57 The ATO reported that improvements in its data and analytics capabilities had enabled tailoring of its approaches to manage cash and hidden economy risk.⁶⁴ Behavioural strategies ranging from support, help and education through to enforcement and prosecution actions had been developed to target high risk sectors—cafés and restaurants, hair and beauty, building and construction, and online sellers.⁶⁵
- 2.58 Other methods deployed overseas involved rewarding good behaviours. BETA advised that a number of jurisdictions in Europe including Slovakia, Italy, Portugal, Greece, Austria and Romania had either experimented with, or are planning to introduce, lotteries tied to sales receipts at the point of sale.⁶⁶ The BETA submission reported that Portugal’s lottery scheme saw an increase in tax receipts of 40 per cent, with revenue growing from 2.5 per cent to 9.5 per cent in 2013 compared with the previous year.⁶⁷
- 2.59 The ATO’s use of behavioural insights in tax administration will be discussed further in Chapter 4, which explores the approach’s potential to foster willing participation.

Tax simplification and technology

- 2.60 Taxpayer obligations in Australia can be distilled down to registration, lodgement, reporting and payment which applies regardless of entity type—an individual, large company or small or medium enterprise. The ATO advises:

All taxpayers are required to apply for a Tax File Number (TFN) and the majority need to lodge an annual tax return. Businesses must also register for an Australian Business Number (ABN) and lodge regular Business Activity

⁶³ OECD, *Tax Administration 2017*, p. 61.

⁶⁴ ATO *Submission 15*, p. 16.

⁶⁵ ATO, *Submission 15*, p. 18.

⁶⁶ Customers would be entered into a lucky draw, with cash prizes, as a reward for demanding tax receipts for goods and services purchased. See Behavioural Economics Team of the Australian Government (BETA), *Submission 18*, p. 6.

⁶⁷ BETA, *Submission 18*, p. 7.

Statements (BAS). The more complex or large-scale your affairs, the more likely there are to be additional reporting or payment requirements.⁶⁸

- 2.61 Australia is among most other advanced economies in relying on tax withholding at source arrangements to collect individual income tax on employment income. This system, in which employers and financial institutions are obligated to withhold an amount of tax from income payments to taxpayers, has been described by the OECD as the ‘cornerstone of an effective tax system’.⁶⁹
- 2.62 Tax regimes may operate as cumulative and non-cumulative withholding systems. Australia, Canada and the United States are examples of countries with a non-cumulative form of withholding tax, in which an annual tax return is submitted to determine the taxpayer’s final tax liability and any tax funds refundable or payable. Ireland, New Zealand and the United Kingdom use cumulative systems whereby the majority of taxpayers do not have to lodge a return.⁷⁰
- 2.63 As discussed above, the pre-filing of third party tax information and the digitisation of assessment and lodgement processes has streamlined tax administration and the taxpayer experience in both types of system.⁷¹
- 2.64 Over the last decade this ‘customer oriented business approach’, combined with advanced analytics and the use of big data, has in the OECD’s view enabled a ‘general rethinking of how tax compliance can best be assured at lowest cost and least burden including through the use of third parties’.⁷² This in turn has enabled some nations, such as Finland and New Zealand, to conduct a wider transformation of their entire tax operation.⁷³

⁶⁸ ATO, *Submission 15*, p. 3.

⁶⁹ OECD, *Tax Administration 2015*, p. 297, cited in Mr Richard Highfield, *Submission 6*, p. 4.

⁷⁰ Mr Richard Highfield, *Submission 6*, p. 4.

⁷¹ Denmark, Norway and Sweden, for example, are non-cumulative withholding systems but have an end-year tax reconciliation process which is fully automated. The United Kingdom and New Zealand, with cumulative tax withholding systems and tax payable at source, have also progressed to an automated approval process for most taxpayers, see Mr Richard Highfield, *Submission 6*, p. 4.

⁷² OECD, *Tax Administration 2017*, p. 48.

⁷³ Finland, for example, initiated a four stage renewal of operations with the aim of ‘redeveloping tax processes, reviewing its tax legislation and replacing seventy current IT applications with one COTS (commercial off the shelf) application’, see OECD, *Tax Administration 2017*, p. 49.

- 2.65 CAANZ's Mr Peter Vial, New Zealand Country Head and Tax Leader, advised that New Zealand's wholesale system redesign, initiated in the late 1980s and 90s, had enabled reductions in tax rates, the introduction of a comprehensive GST, increases in social assistance, and reduction of workplace expenses and other entitlements. Today, only a third of the three and half million taxable New Zealanders lodge annual income tax returns.⁷⁴
- 2.66 Mr Vial further advised that technical advances in pre-filing, combined with planned law reform to support real-time information sharing, could further reduce the number of people needing to lodge a tax form:

These proposals, if implemented, will allow Inland Revenue to issue refunds or confirm tax to pay based on the information it holds from banks, from employers and from New Zealand companies that are paid the taxpayer dividend... Those proposals follow some draft legislation that is before our parliament at the moment that provides for Inland Revenue to receive income information from employers and banks more quickly and more frequently so that earlier and more regular information from the banks and employers will allow the social assistance entitlements to be adjusted up or down in something more like real-time, and more people will therefore be out of the tax return process.⁷⁵

- 2.67 However, the Inspector-General of Taxation cautioned that the potential to conduct wholesale tax reform depends on the 'different socio-economic and legal frameworks in each system', for example, 'in many countries where tax returns are fully completed by the revenue authority, there may not be as comprehensive a regime for claiming deductions for work-related expenses as there is in Australia.'⁷⁶
- 2.68 Professor Hiscox, Head of BETA, took a similar view on the potential to shift to full system automation:

I was very recently talking with the ATO about the comparisons between the Swedish system and the Australian system... we have complexities in our system that make it a little bit harder to do that here than in a place like Sweden—how we treat work related expenses and things like that. So making

⁷⁴ Mr Vial, CAANZ, *Committee Hansard*, Melbourne 17 July 2017, pp. 1, 2.

⁷⁵ Mr Vial, CAANZ, *Committee Hansard*, Melbourne 17 July 2017, pp. 1, 2.

⁷⁶ IGT, *Submission 5*, p. 26.

things easier or simplification interventions like pre-filing are a little bit more challenging in our context.⁷⁷

Co-operative compliance

2.69 Global co-operation and harmonisation on tax matters is occurring in a number of spheres. This section briefly considers the implications for tax administration of recent information sharing agreements and tax legislation reforms.

2.70 In particular, the OECD tax administration report identifies moves to address large business tax avoidance under implementation of the OECD/G20 Base Erosion and Profit Shifting (BEPS) project as a factor in driving significant change in tax administration.⁷⁸ The ATO website reports that conservative OECD estimates indicate that annual revenue loss due to BEPS is between \$100 to \$240 billion USD Base, explaining that:

Base erosion and profit shifting (BEPS) refers to the tax planning strategies used by multinational companies to exploit gaps and differences between tax rules of different jurisdictions internationally to artificially shift profits to low or no-tax jurisdictions where there is little or no economic activity.⁷⁹

2.71 CPA Australia's Mr Paul Drum referred to BEPS's relevance in the context of the emergence of the digitisation of the global economy:

The G20 and the OECD have just been working through the base erosion profit-shifting [BEPS] agenda to revisit tax treaties, to look at the digital economy, country-by-country reporting and information-sharing between tax jurisdictions. Some of these are watershed moments in the history of countries and tax systems in international tax.⁸⁰

2.72 The OECD report highlighted BEPS as a major advance in co-operative compliance, noting:

...co-operative compliance approaches are built on the mutual interests and established processes of the parties they are able to readily respond to changes in legislation or regulation. This has seen them already being adapted to

⁷⁷ Professor Hiscox, BETA, PM&C, *Committee Hansard*, Canberra, 10 May 2018 p. 17.

⁷⁸ OECD, *Tax Administration 2017*, p. 2.

⁷⁹ATO, Base Erosion and Profit Shifting (BEPS) <www.ato.gov.au/business/international-tax-for-business/in-detail/base-erosion-and-profit-shifting/> viewed 25 January 2018.

⁸⁰ Mr Paul Drum, Head of Policy CPA Australia, *Committee Hansard*, Melbourne, 17 July 2017, p. 12.

accommodate the requirements of initiatives like country-by-country reporting and other outcomes from the OECD/G20 Base Erosion and Profit Shifting (BEPS) project into the TCF of the taxpayer and into the risk assessment systems of tax administrations.⁸¹

2.73 The OECD, however, also saw a risk for tax administrators under implementation of global information sharing agreements. In particular, it referred to the introduction of the Common Reporting Standard (CRS), which calls on jurisdictions to obtain information from their financial institutions and automatically exchange that information with other jurisdictions on an annual basis.⁸² The ATO has advised of Australia's obligations under the CRS:

The Common Reporting Standard (CRS) is the single global standard for the collection, reporting and exchange of financial account information on foreign tax residents. Banks and other financial institutions will collect and report to us financial account information on non-residents using the standard. We will exchange this information with the participating foreign tax authorities of those non-residents. In parallel, we will receive financial account information on Australian residents from other countries' tax authorities. This will help ensure Australian residents with financial accounts in other countries comply with our tax law and deter tax evasion.⁸³

2.74 The OECD highlighted its concerns about the potential digital burden for tax administrators sharing information under the CRS as they move to full automation and pre-filing:

Due to the fact that pre-filing of tax returns requires a high degree of certainty, in the early days of exchange under a new standard such as the CRS, tax administrations may exercise caution before using the data in pre-filing tax returns until they are sufficiently confident about the quality of the data and the matching of that data against individual taxpayers.⁸⁴

⁸¹ OECD, *Tax Administration 2017*, p. 2.

⁸² OECD, The Common Reporting Standard (CRS), was developed in response to the G20 request and approved by the OECD Council on 15 July 2014. <www.oecd.org/tax/automatic-exchange/common-reporting-standard/> viewed in 21 December 2017.

⁸³ ATO, Common Reporting Standard (CRS) <www.ato.gov.au/Business/Large-business/In-detail/Business-bulletins/Articles/Common-Reporting-Standard/> viewed 25 January 2018.

⁸⁴ OECD, *Tax Administration 2017*, p. 195.

2.75 Accordingly, it recommended that jurisdictions give careful consideration to what is ‘sufficient data’ to provide an accurate assessment using pre-filing, cautioning:

Significant gaps can also lead to significant non-compliance. This can either be because the taxpayer does not believe that the tax administration has access to the data or the taxpayer just assumes that the amount assessed is accurate.⁸⁵

Use of tax professionals

2.76 Australia has one of the highest levels of reliance on tax practitioners of any OECD country. At hearings, the Tax Commissioner Mr Chris Jordan AO advised that Australia’s reliance on agents is second only to Italy.⁸⁶

2.77 The Tax Practitioners Board cited data from the Inspector-General of Taxation’s 2015 report on the ATO’s services and supports to tax agents, to confirm that:

[Australia’s use of tax agents at] current levels are among the highest in OECD countries, exceeding those of Canada (39 per cent), the United States of America (40 per cent), New Zealand (50 per cent) and the United Kingdom (67 per cent).⁸⁷

2.78 The submission from the Inspector-General highlighted the results of a 2008 OECD comparative study to support its view that tax agents play a ‘crucial intermediary role’ between taxpayers and the revenue authorities:

The importance of the role tax advisers play in a tax system can be tested by answering a simple question: would compliance with tax laws improve if tax advisers did not exist? The Study Team found no country where the answer to that question is yes. Across the whole range of taxpayers, taxes and circumstances, the vast majority of tax advisers help their clients to avoid errors and deter them from engaging in unlawful or overly-aggressive activities.⁸⁸

2.79 The ATO submission provided a sectoral breakdown of tax agent usage by Australian taxpayers:

⁸⁵ OECD, *Tax Administration 2017*, p. 194.

⁸⁶ Mr Chris Jordan AO, Tax Commissioner, *Committee Hansard*, Canberra, 29 March 2017, pp. 2, 8.

⁸⁷ Cited in Board of Taxation, *Submission 9*, p. [2].

⁸⁸ IGT, *Submission 5*, p. 15.

In Australia, most individuals and businesses (74 per cent of all entities) use a tax professional to help them comply with their obligations. 68 per cent of individuals not in business lodge their annual tax return through a tax agent, 95 per cent of small businesses use an agent for their annual return and a substantial number also use a BAS agent for their PAYG and GST obligations.⁸⁹

2.80 Mr Graeme Davis, Treasury's Acting Division Head, Tax Framework Division, conjectured that tax complexity may be one cause for Australia's very high reliance on tax agents compared with other nations. However, he emphasised that 'there doesn't seem to be a direct correlation' between tax complexity and agent usage, citing the lower tax agent usage in the United States which is not known for having a simple tax system.⁹⁰ Mr Davis also suggested that a more nuanced consideration of taxpayer reliance on agents in different jurisdictions may influence data for comparisons, saying:

One of the questions that is worth asking is: different tax systems work quite differently, and what do tax agencies do in different systems? They are not the same thing in each system. In our system, the tax agents are fulfilling a number of functions. So they are filling a function of helping people get their tax returns in...some people are making use of that—you have a longer time to get your return in... but for business they are also helping them run their businesses to some extent...they are using someone to help them with their accounting...So it may not show up that way in other jurisdictions. So one of the challenges is looking at that data and asking: is that actually comparable?⁹¹

2.81 The Committee considered that while complex systems such as that in the United States are often cited to discount the impact of tax complexity in Australia on agent use, it is important to note that this complexity is mostly felt by companies and not individual taxpayers, while tax agent use remains high across the spectrum.

2.82 Tax agent use and tax complexity is discussed in more detail in Chapter 5.

⁸⁹ Australian Taxation Office, *Submission 15*, p. 3.

⁹⁰ Mr Graeme Davis, Acting Division Head, Tax Framework Division, The Treasury, *Committee Hansard*, Canberra, 29 March 2017, pp. 14–15,

⁹¹ Mr Davis, The Treasury, *Committee Hansard*, Canberra, 29 March 2017, p. 14.

Emerging challenges

Cash economy

- 2.83 The OECD uses the term ‘the non-observed’ economy to represent all economic activity that goes unreported (for a variety of reasons) in normal statistical data gathering processes used for estimating gross domestic product and other important aggregates of economic activity.⁹²
- 2.84 The Australian Bureau of Statistics (ABS) has adopted this definition, as well as the OECD’s breakdown of the constituents of the ‘non-observed economy’, for further analysis:
- 1 **Underground production:** Activities that are productive and legal but are deliberately concealed from public authorities to avoid payment of taxes or compliance with regulations.
 - 2 **Illegal production:** Productive activities that generate goods and services forbidden by law or that are unlawful when carried out by unauthorised procedures.
 - 3 **Informal sector production:** Productive activities conducted by unincorporated enterprises in the household sector or other units that are unregistered and/or less than a specified size in terms of employment, and that have some market production.
 - 4 **Production of households for own-final use:** Productive activities that result in goods or services consumed or capitalised by the households that produced them.
 - 5 **Statistical underground:** Defined as all productive activities that should be accounted for in basic data collection programs but are missed due to deficiencies in the statistical system.⁹³
- 2.85 Definitions of the cash economy can be inclusive or exclusive of these components. The Australian Government’s interim report on the black economy, for instance, acknowledged but excluded assessment of illegal and illicit activity, whereas the final report included crime, illegality and illicit product sales.⁹⁴

⁹² Mr Richard Highfield, *Submission 6*, p. 15.

⁹³ Mr Richard Highfield, *Submission 6*, p. 15.

⁹⁴ Further discussion of the definition is in Chapter 5 of this report.

- 2.86 The OECD report refers to the distinction in discussing the shadow or underground economy, noting that it was the subject of a comprehensive information note prepared by the FTA in 2012 *Reducing Opportunities for Tax Non-compliance in the Underground Economy* (OECD, 2012b). This note explored the key components of successful compliance strategies, assessed the impact of digital payment technologies and reviewed the methodology for estimating the size of the underground economy. The OECD also refers to the recently released report *Technology Tools to Tackle Tax Evasion and Tax Fraud* (OECD, 2017), which drew on the experience of 21 jurisdictions to highlight their key successes in using technology to help tackle tax evasion.⁹⁵
- 2.87 As discussed previously, advanced data analysis is being conducted in a number of jurisdictions to better identify areas of high risk for cash economy activity and revenues evasion, including where this intersects with criminal activity. Jurisdictions have also adopted a range of methodologies to assess the size of the tax gap associated with cash activity, with some attempting an estimate of losses associated with tax related illicit activity, such as through money laundering.⁹⁶
- 2.88 The Australian Transaction Reports and Analysis Centre (AUSTRAC) is Australia's financial intelligence agency and the central data source for monitoring of tax evasion.⁹⁷ Mr David Hawkins of AUSTRAC's Strategic Intelligence and Policy section advised of the 100 million 'incoming and outgoing wire transfers' received by his agency in 2016 for this purpose. He also highlighted AUSTRAC's sharing of information online with all its partner agencies, in contrast to similar agencies in many other countries.⁹⁸
- 2.89 The Inspector-General of Taxation's submission listed a range of approaches to reduce cash activity adopted by other revenue authorities reporting to the OECD:
- Comprehensive industry benchmarking, coupled with leveraging via tax professionals, media engagement and automated targeting of large numbers of taxpayers (Australia).

⁹⁵ OECD, *Tax Administration 2017*, pp. 59–60.

⁹⁶ OECD, *Tax Administration 2017*, pp. 62–63.

⁹⁷ Mr Daniel Mossop, Director, Financial Crime Section, Attorney-General's Department and Mr David Hawkins, Acting National Manager, Strategic Intelligence and Policy, Australian Transaction Reports and Analysis Centre (AUSTRAC), *Committee Hansard*, 21 June 2017, p. 2.

⁹⁸ Mr Hawkins AUSTRAC, *Committee Hansard*, Canberra, 21 June 2018, p. 5.

- Industry-based withholding/third party reporting regimes (Ireland and Canada).
- Increased controls over cash transactions (Netherlands, Spain, and Sweden).
- Increased record-keeping controls for employees in high-risk industry sectors (e.g. restaurants and hairdressing) (Sweden's staff ledgers).
- Initiatives aimed at reducing the use of cash transactions (Norway and Turkey).
- The use of monetary incentives to encourage proper record-keeping and deter unrecorded cash payments (Canada's and Norway's home renovation tax credit, Korea's lottery and incentive for obtaining receipts).
- Increased revenue body use of suspicious transactions reports collected by a separate government agency (Australia and France).
- Educating new/potential taxpayers (Austria's schools initiative, Canada's trade school initiative).⁹⁹

2.90 **Appendix D** provides a tabular presentation of methods implemented (or planned to be implemented) by tax administrators and law-makers overseas.¹⁰⁰ The cash economy, and the associated tax gap, is discussed in Chapter 5.

The changing workforce

2.91 Another factor informing approaches to cash activity and non-compliance are the tax and compliance implications of the emerging sharing or gig economy. The OECD warns:

The global sharing economy, which puts suppliers and customers in direct contact through web or mobile based applications, presents an emerging tax risk. Because of the private nature of payments, and the often global basis for payments, it can be challenging to ensure tax compliance. To overcome this, tax administrations are increasingly reaching out to other government agencies and other tax administrations to ensure comprehensive exchanges of information relating to transactions between individuals based in different jurisdictions. In Australia, for example, the Australian Tax Office (ATO) has access to information on financial flows maintained by the Australian

⁹⁹ Cited in IGT, *Submission 5*, pp. 7–8.

¹⁰⁰ Board of Taxation, *Submission 17*, Annex A: The Overseas Experience.

Transaction Reports and Analysis Centre. This helps the ATO identify unregistered businesses operating in the sharing economy (OECD, 2017).¹⁰¹

2.92 The submission from the Institute of Public Accountants (IPA) reported that in Australia contracting has increased to 10 per cent of the workforce. Drivers of this are the growth in the sharing economy through online IT and mobile use, and incentives provided to employers and contractors under the tax system. These include greater employment deductibility, lower taxes and the potential for income splitting.¹⁰² IPA concluded that ‘the growing number of self-employed businesses acting as contractors poses to the ATO a greater risk of losing tax revenue when compared to collecting PAYG from employed individuals’.¹⁰³

2.93 The recent UK review *Good Work, The Taylor Review of Modern Working Practices*, July 2017, noted:

The labour market is changing, self-employment is rising, innovative forms of working are causing us to question established norms and how our current legislative framework fits with these developments. These changes have impacts for ordinary people, who may be less certain about their rights, or who might feel that the system doesn’t accommodate the reality of their working relationships. It also has impacts for the state, which sees the fiscal impact of rising self-employment and incorporation.¹⁰⁴

2.94 The report considered that a clearer distinction between an ‘employee’ and a ‘dependent contractor’ was needed, suggesting:

The status of ‘dependent contractor’ should have a clearer definition which better reflects the reality of modern working arrangements, properly capturing those more casual employment relationships that are on the increase today – an individual who is not an employee, but neither are they genuinely self-employed.¹⁰⁵

2.95 The review recommended that, in developing the new ‘dependent contractor’ test, renewed effort should be made to align:

¹⁰¹ OECD, *Tax Administration 2017*, p. 62.

¹⁰² IPA, *Submission 2*, p. 3.

¹⁰³ IPA, *Submission 2*, p. 3.

¹⁰⁴ Government of the United Kingdom (UK), *Good Work: the Taylor Review of Modern Working Practices*, Independent report, 11 July 2017, p. 6. <www.gov.uk/government/publications/good-work-the-taylor-review-of-modern-working-practices> viewed 25 January 2018.

¹⁰⁵ Government of the UK, *Good Work: the Taylor Review of Modern Working Practices*, July 2017, p. 36.

- the employment status framework with the tax status framework to ensure that differences between the two systems are reduced to an absolute minimum, and
- Government should develop and create a free to use online tool that provides individuals with an indication of their employment status, similar to the Employment Status Indicator tool for tax purposes.¹⁰⁶

Committee conclusion

- 2.96 Tax administrations are undergoing a process of sustained review and reform under the imperatives of globalisation, technological change and budgetary pressures.
- 2.97 The OECD has stated that the increased usage by taxpayers of digital products and services demands that tax agencies respond by digitising and simplifying tax administration systems. Ostensibly this is a rational response to the accelerated demands of daily life and business in a globalised economy. However, these measures also provide revenue agencies and governments with opportunities to reduce investment in people—experienced and expert staff, auditors, and other services, while encouraging voluntary engagement by taxpayers.
- 2.98 As part of the evolution of this ‘tax eco-system’—or ‘natural’ network of engagement between individual tax payers, government agencies and businesses—there are incentives to support the community’s tax and financial literacy, both online and in person, and to develop compatible interfaces with private sector products. The next phase is the proliferation of payment apps and point of sale mechanisms to achieve real-time sales monitoring and tax registration. These things equally assist tax payers under the same rationale—making compliance easier, and are being adopted by comparable revenue agencies around the world.
- 2.99 Significantly, the development of advanced data analysis, identity verification and information sharing techniques provides revenue agencies and their partners with powerful new tools for tax monitoring and catching criminal non-compliance and deliberate under-reporting. Technical innovation therefore also supports a higher degree of surveillance of individuals and businesses, and through information sharing globally, the

¹⁰⁶ Government of the UK, *Good Work: the Taylor Review of Modern Working Practices*, July 2017, pp. 38, 39.

potential, as the OECD has observed, to reduce the capacity to vet the accuracy of incoming pre-filled information and overwhelm tax administrators.

- 2.100 The ATO, in most areas, is on par with other nations in working , sharing goals to modernise tax administration services and develop technical solutions to new challenges. Areas of strength include the ATO's work with the OECD on Application Programming Interfaces (APIs), by which e-invoicing and other electronic systems and products communicate securely. Less advanced are applications for real-time payment apps and immediate tax registration, which the Australian Government has not prioritised, nor any move made at this point towards a majority non-lodgement system as deployed in some comparable nations. Australia's high reliance on tax agents, as key partners in the tax system, is another area for consideration.
- 2.101 This chapter has provided a standard of international best practice for comparison of ATO service delivery in key areas, which is examined in more detail in the following chapters of this report.

3. How taxpayers engage

Introduction

- 3.1 The Australian Tax Office (ATO) aims to foster and support a tax system where 'Australians value the tax and superannuation systems as community assets, where willing participation is recognised as good citizenship'.¹
- 3.2 Australian taxpayers primarily engage with the tax system during three key activities:
- during income derivation and reporting (and payment of salaries/wages and superannuation contributions);
 - when purchasing goods and services; and
 - in reconciling their tax obligations on income earned during a taxable period² (directly, or through a tax agent).
- 3.3 This chapter considers how taxpayers currently engage with Australia's taxation and superannuation systems. It covers the ATO's processes for interaction with taxpayers, in particular, with individuals and small business,³ and the design and refinement of user friendly software systems,

¹ Australian Public Service Commission (APSC), *Capability Review: Australian Taxation Office*, May 2013, p. 5. As mentioned in Chapter 1, official information guides for new Australian residents are silent on tax obligations and fair expectations.

² The Australian financial year ends 30 June.

³ As stipulated by the terms of reference.

tools and products to improve accuracy and taxpayer compliance. While it does not, in any detail, discuss specific tax regulation, the nature of Australia's tax system and how this impacts willing participation is discussed.

- 3.4 Finally, the chapter considers the likely re-definition of the role of tax intermediaries in response to these factors going forward. The use of behavioural insights and education to support voluntary engagement, and future challenges and opportunities for tax regulation are dealt with in following chapters of the report.

Stakeholders in tax engagement

- 3.5 Four key stakeholder groups engage in Australia's taxation system for individuals and small business—employees and employers, sole traders and tax professionals. The ATO also manages tax engagement with five other main client groups, comprising privately owned and wealthy groups; public companies and international businesses; not-for-profit organisations; superannuation funds, and tax professionals and other intermediaries.⁴
- 3.6 As indicated by the terms of reference for this inquiry, this chapter will focus on the effectiveness of the ATO's systems for engagement primarily with individuals and small businesses, and on its work with tax professionals.

Employees and employers

- 3.7 A key feature of Australia's tax system is the use of unique engagement identifiers—for example, for individuals, a Tax File Number (TFN), and for businesses, an Australian Business Number (ABN). There are various implications if you do or don't have, or don't quote one of the identifiers in the system. As such, there are incentives to register in the tax system.
- 3.8 The majority of Australian taxpayers are individuals,⁵ mostly salary or wage earners⁶ who have taxes remitted from their regular pay by their employer to the ATO.

⁴ Australian Taxation Office (ATO), *Commissioner of Taxation Annual Report 2016–17* (hereafter ATO Annual Report 2016–17), p. 12.

⁵ Over the 2014–15 income year, 83.8 per cent of taxpayers in Australia were individuals (13 213 814 of 15 766 359 taxpayer entities). See ATO *Taxation Statistics, All Tax Returns, Table 1: Size of Entities, 2014–15 Income year* (NB includes data up to 31 October 2016) <www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Taxation-statistics/Taxation-statistics-2014-15/?anchor=alltaxreturns#alltaxreturns> viewed 27 February 2018.

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- 3.9 At the end of a financial year taxpayers are required to reconcile their tax paid on taxable income earned in the period and report this to the ATO by 31 October following the end of the financial year.⁷
- 3.10 Prior to the cessation of printed 'TaxPacks'⁸ Pay As You Go (PAYG) employee taxpayers had limited direct contact with the tax administrator. Tax Packs were delivered to Australian households when self-assessment commenced—reflecting the complexity of the Australian taxation system—and ceased in 2012⁹ with the advent of internet based tax lodgement (myTax) and on-line support resources. The myTax system is part of the myGov website, and unlike the eTax¹⁰ system it replaced, the operation of myTax relies on internet connectivity during use.
- 3.11 TaxPack delivery once prompted the consideration and reconciliation of tax affairs by individuals directly, or prompted engagement of a tax agent. These sorts of prompts are now delivered via digital mechanisms.
- 3.12 Australian individuals have incentive to complete their returns by the specified due date to receive a tax refund or avoid being fined for not paying taxes assessed. Submitting a tax return results in an assessment of tax

⁶ In 2010–11, a total of 10 039 401 Australians who lodged tax forms reported income from wages and salaries. This approximated \$521.3 billion or 80.6 per cent of total income (from all sources). See Australian Bureau of Statistics (ABS), 'Wage and Salary Earner Statistics for Small Areas', *Time Series, 2010–11, cat. no. 5673.0.55.003*, released 20 December 2013. (Last revision of dataset series.) <www.abs.gov.au/ausstats/abs@.nsf/mf/5673.0.55.003#Anchor2> viewed 27 February 2018.

⁷ Section 161(1) of the *Income Tax Assessment Act 1936* (ITAA 1936) provides that: 'Every person must, if required by the Commissioner by notice published in the Gazette, give to the Commissioner a return for the year of income within the period specified in the notice'. The 2009 review report of the Inspector General of Taxation (IGT) *Review of the Non-Lodgement of Individual Income Tax Returns* (p. 11) notes that exceptions to lodgement 'are few, so that effectively all individual Australian taxpayers with taxable income in excess of the prescribed threshold amount ... are required to lodge a return'. See <igt.gov.au/publications/reports-of-reviews/non-lodgement-of-individual-income-tax-returns/chapter-3-overview-of-income-tax-return-lodgement-within-australia/> viewed 13 February 2018.

⁸ Printed tax return instructions and forms which guided taxpayers with 'simple tax affairs' to complete paper tax returns. The packs were also available at Tax Office locations and at newsagencies.

⁹ Replaced with a shorter instruction guide and phased out, eventually ceasing to be sent to households by 2015.

¹⁰ An electronic version of a paper form which was supported by an electronic tax return guide.

liability for the period, at a time after lodgement.¹¹ Taxes may then be refunded directly to the taxpayer or a tax payment obligation is raised.

- 3.13 Employers are required to calculate PAYG tax and superannuation deductions¹² and withhold and remit their employees' tax deductions and superannuation components to the relevant entities in a timely fashion. Employee compliance costs for business can be significant.

PAYG arrangements scheme

- 3.14 The PAYG arrangements scheme allows taxpayers to meet their predicted tax liabilities by making progressive payments as income is earned during a financial year. This regime reduces the likelihood of a large tax bill at year end and provides government with a steady stream of tax revenue during the accounting period. The PAYG scheme was established in July 2000, replacing a number of reporting schemes and as such designed to provide both an instalment scheme *and* a withholding tax system.

PAYG withholding system

- 3.15 The withholding system requires an employer who makes a payment to a taxpayer for work, such as salary or wages, to withhold an amount from the payment and to remit it to the ATO.¹³
- 3.16 PAYG employee taxpayers usually do not directly engage with the ATO until it is time to reconcile their taxes paid with income derived from all sources. Importantly, however, these taxpayers have already engaged with the tax system, albeit indirectly, through the regular remittances of income tax from their pay.¹⁴
- 3.17 In January of this year the Inspector-General of Taxation reported on the *Review into Aspects of the Pay As You Go Instalments System* which highlighted,

¹¹ Tax return assessment turnaround times have declined with more automated systems and now digitalised returns. The ATO website stated at Tax Time 2017 that 'We aim to process paper tax returns within 50 business days of being received. If you lodged online using myTax, most refunds are processed in 2 weeks or less', see <www.ato.gov.au/Individuals/Lodging-your-tax-return/In-detail/Your-notice-of-assessment/> viewed 27 February 2018.

¹² Often varying hours and rates.

¹³ The types of payments for work from which amounts must be withheld are summarised in Division 10 of Schedule 1 to the *Tax Administration Act 1953*.

¹⁴ The *Taxation Administration Act 1953* schedule 1, s 6-1 details the scheme requiring periodic reporting and pre-payment of income taxes.

through feedback to the inquiry, the automated nature of PAYG tax engagement, and also the lack of community understanding of the tax system.¹⁵

- 3.18 Mr Richard Highfield, a tax system expert and former Deputy Commissioner at the ATO, highlighted the superiority of the PAYG withholding system, which ‘relies on the use of withholding at source arrangements to collect individual income tax on employment income’, and noting that: ‘There is considerable international experience that draws attention to the superiority of collecting income tax in this way’.¹⁶

PAYG instalments

- 3.19 Most taxpayers who earn business or investment income which is not subject to withholding at source¹⁷ are required to pay periodic instalments towards their annual income tax liability. Once registered in the PAYG instalments system taxpayers receive an Activity Statement from the ATO setting out the taxpayer’s instalment amount.¹⁸
- 3.20 Individual taxpayers who have additional tax reporting obligations, for example for the Goods and Services Tax (GST), are required to report their PAYG instalments on a Business Activity Statement.¹⁹

Superannuation obligations

- 3.21 Under the *Superannuation Guarantee (Administration) Act 1992* compulsory employer contributions, currently 9.5 per cent,²⁰ are regulated to be paid to a

¹⁵ IGT, *Review into Aspects of the Pay As You Go Instalments System*, Inspector-General of Taxation, January 2018, p. v <<http://igt.gov.au/publications/reports-of-reviews/aspects-of-the-pay-as-you-go-instalment-system-review/>> viewed 27 February 2018.

¹⁶ Mr Richard Highfield, *Submission 6*, pp. 3–4.

¹⁷ Examples of withholding at source include for GST in trade of goods or services of a sole trader.

¹⁸ This is based on their previous year’s income tax liability adjusted by likely growth in Australia’s Gross Domestic Product (GDP). Instalment amounts are generally quarterly payments made directly to the ATO. See IGT, *Review into Aspects of the Pay As You Go Instalments System*, January 2018, p. 2.

¹⁹ IGT, *Review into Aspects of the Pay As You Go Instalments System*, January 2018, p. 5.

²⁰ The super guarantee contribution regime applies to all employed Australians aged 18 and over, and earning at least \$450 per month from a given employer.

mySuper fund (regulated designated superannuation fund)²¹ and calculated on an employee's ordinary time earnings, paid on top of those earnings. The Superannuation Guarantee (SG) payments are now due to be paid to the selected fund every quarter.

3.22 Industry Super Australia prepared a report in December 2016 which highlighted a significant level of employer non-compliance with the required contribution rules, estimated to be \$3.6 billion in the 2013–14 fiscal year.²² The ATO administers major aspects of Australia's superannuation system including the SG scheme and the superannuation co-contribution scheme. It is the regulator of 597 000 self-managed super funds (SMSFs) and supports approximately 250 APRA-regulated²³ superannuation funds which have 34.5 million member accounts receiving contributions and paying benefits.²⁴

3.23 The Senate Standing Committee on Economics inquired into lost SG contributions, tabling its report *Superbad – Wage Theft and Non-compliance of the Superannuation Guarantee*²⁵ in May 2017. It found one of the causes of unpaid SG payments was the misclassification of workers as contractors. This issue also affects tax engagement and is discussed in Chapter 6. The Senate Committee report explained:

Generally speaking, if a worker is classified as an employee, their employer has the liability to pay SG. However, if a worker is classified as a contractor, this is not the case. However, it can be complicated for an employer to correctly classify their workers for SG purposes, particularly as the definition of an employee in common law differs from the expanded definition provided in the SGA Act.²⁶

²¹ Details of mySuper at Treasury <treasury.gov.au/programs-and-initiatives-superannuation/mysuper/> viewed 27 February 2018.

²² Industry Super Australia/Cbus, *Overdue: Time for Action on Unpaid Super*, Report, December 2016.

²³ Australian Prudential Regulation Authority (APRA)

²⁴ ATO Annual Report 2016–17, p.49.

²⁵ Australian Senate Standing Committee on Economics, *Superbad – Wage Theft and Non-compliance of the Superannuation Guarantee*, May 2017.

²⁶ Australian Senate Standing Committee on Economics, *Superbad – Wage Theft and Non-compliance of the Superannuation Guarantee*, May 2017, p. 40.

3.24 As the Inspector-General of Taxation pointed out in the Senate inquiry:

There are inherent difficulties associated with the employee/contractor distinction which stems from its common law definition of 'employee' with no determinative factor. There are a number of factors which have to be considered relative to each other, making a determination very much reliant on the facts of each case.²⁷

3.25 The Senate Economics Committee recommended that the Government investigate options to extend the ATO's current private binding advice and administratively binding advice frameworks and make them available to workers as well as to businesses so as to clarify the definition of employee for SG purposes.²⁸

3.26 The correct and timely payment of superannuation contributions for genuine employees is fundamental to Australia's retirement savings. As such, engagement in the super system is as important as is tax compliance for employees.

3.27 The ATO's role in the superannuation sector is to ensure willing participation through:

- Correctly registering new SMSF registrants on eligibility and advising of trustee obligations—this can be done via ATO Online which is accessed via myGov;
- Lodging timely annual returns information and for APRA-regulated funds, their Member Contribution Statements on time;²⁹
- Reporting complete and accurate information (all SMSFs must be independently audited); and, importantly,
- Paying tax obligations on time.³⁰

3.28 The ATO provides tailored support and services for SMSFs including guidance on specific compliance issues through every stage of the fund's life-cycle. The ATO's 2017 client satisfaction survey found that SMSFs were

²⁷ Australian Senate, Standing Committee on Economics, *Superbad – Wage Theft and Non-compliance of the Superannuation Guarantee*, May 2017, p. 40.

²⁸ Australian Senate, Standing Committee on Economics, *Superbad – Wage Theft and Non-compliance of the Superannuation Guarantee*, May 2017, p. 42.

²⁹ For 2015-16 SMSF annual returns, which were due 2016-17, 93 per cent were on time while during 2016-17, 97 per cent of APRA regulated funds lodged income tax returns on time. *Commissioner of Taxation Annual Report, 2016-17*, p. 49.

³⁰ ATO Annual Report 2016–17, pp. 50, 51.

significantly more satisfied with the ATO's online services than they were with their pre-digital offerings.³¹ In addition, the ATO provided significant support for APRA-regulated funds during the SuperStream introduction.

- 3.29 Nevertheless, statistics in the section indicating high levels of employer non-compliance with the super contribution rules is concerning to the Committee. The Committee would support consideration of other proposals to improve compliance, such as making superannuation payments more regular, potentially in line with wage payments, and requiring superannuation funds to provide regular balance information so that beneficiaries can better determine what they are getting paid and when.

Small business

- 3.30 Small businesses are required to lodge a Business Activity Statement (BAS) and make payments for GST, PAYG withholding tax and SG contributions for employees, PAYG instalments, some Fringe Benefits Tax (FBT) and other incidental taxes.³² There are many tax trigger points where they need to explicitly engage with the tax and super system.
- 3.31 Small business owners comprise new-starters, many with no business background or accounting acumen and yet there are numerous regulatory and tax-related registrations and requirements in the architecture of business activities. As also outlined in Chapter 4, the ATO provides tax obligation and associated business supports for small business but for many the support of a trusted tax and accounting professional is required. As such, most small businesses employ accountants who also manage their tax affairs.
- 3.32 Small businesses may be sole traders who, as of Tax Time 2016, had the opportunity to utilise myTax to prepare their tax return if they had simple tax affairs.³³ Sole Traders could also access the myDeductions app for the first time in December 2016.

³¹ ATO Annual Report 2016–17, p. 51. This is despite the system failures in December 2016 and February 2017 which the ATO recognise as being a 'challenge.'

³² ATO Annual Report 2016–17, p. 24. 'Small businesses' have an annual turnover of less than \$2 million.

³³ ATO Annual Report 2016–17, p. 27.

Businesses as purchasers and vendors

3.33 Businesses that purchase and sell goods and services subject to the Goods and Services Tax (GST) are required to register once they have reached a threshold of \$75 000 gross business income in any 12 month period.³⁴ Registration is otherwise optional. Once registered, an ABN is allocated which enables transacting within the GST system. Practices of cash acceptance for reduced payment for services so that the income is off-the-books means that not only is taxable income unreported but also the goods and services tax.

3.34 Evidence to the inquiry suggested that the GST regime provided some form of amelioration of cash economy activity merely because to claim back GST input credits a business would need to be working within the regulatory framework. For example, Mr Paul Drum of CPA Australia highlighted this:

...and this is behavioural economics at work—people are quite happy not to pay their income tax, but they are sure as hell going to claim back their input tax credit. So they wanted their 10 per cent back on their business input.³⁵

3.35 He also noted that, fundamentally ‘VATs and GSTs pick up some cash that otherwise would not be picked up, so they invariably pick up cash from the cash economy because people in the cash economy must still consume’.³⁶

3.36 The ‘refund churn’³⁷ created by the GST system was also discussed as it constitutes around half of all refunds in the tax system:

Fifty per cent of GST is actually refunded to taxpayers. It is a very high incidence. But a lot of that arises because you have taxpayers in business in export industries where their goods are exported free of GST. They incur GST when they make purchases, but they do not charge it when they make sales, so they get a refund of that GST. That is a design feature of a value-added tax,

³⁴ Businesses must register within 21 days of reaching this threshold and once registered must include a 10 per cent GST component in the sale of goods or supply of services. Taxi drivers for a fare, irrespective of whether the driver owns the vehicle or not, must register regardless of GST turnover. Refer to the ATO, Registering for GST <[www.ato.gov.au/Business/GST/ Registering-for-GST/#Whendoyouneedtoregister](http://www.ato.gov.au/Business/GST/Registering-for-GST/#Whendoyouneedtoregister)> viewed 2 March 2018.

³⁵ Mr Paul Drum, Head of Policy, CPA Australia, *Committee Transcript*, 18 July, p.11.

³⁶ Mr Drum, CPA Australia, *Committee Transcript*, 18 July 2017, p. 11.

³⁷ A vendor can claim a credit for any GST included in the price paid for inputs used in their business. You claim GST credits in your business activity statement.

and it occurs in many other countries for example—the United Kingdom and Canada as well.³⁸

- 3.37 Other comment on the GST was more general, with reference made to the Australia’s future taxation system (AFTS) review report.³⁹ Mr Richard Highfield described Australia’s complex GST system as one of the ‘elephants in the room’ for Australian tax reform, contrasting it unfavourably with New Zealand’s more comprehensive streamlined approach.⁴⁰
- 3.38 The level of regulatory detail entailed in review of these concerns was beyond the scope of this inquiry but the Committee notes it is an area of consideration for future tax reviews. However, on the broader issue of tax simplification, Mr Matthew Pawson, the 2018 President of the Tax Institute, drew attention to the many GST rulings resulting from tax complexity in this area—a problem also raised by Mr Pier Parisi⁴¹ and ECU Australia.⁴² As such, Mr Pawson advocated against a ‘piecemeal’ review of the tax system:

We have so many exceptions to the rules that it makes it very difficult for taxpayers to understand and for the ATO to administer it. You just have to look at the number of guidance statements that the tax office issues, the public rulings, private rulings—there are thousands of them. I do some lecturing to postgraduate legal practice students. It’s in the space of GST. We’ve only had the GST for 17 years, and there are already over 200 rulings. It’s a minefield of complexity.⁴³

Taxation intermediaries

- 3.39 The inquiry’s explanatory paper advises that there were 75 436 registered tax practitioners in Australia at 30 June 2016.⁴⁴ The 2016–17 annual report of the Commissioner of Taxation notes that 33 800 were registered and active

³⁸ Mr Richard Highfield, Private capacity, *Committee Hansard*, Canberra, 14 June 2017, p. 3.

³⁹ Mr Highfield commented on broadening the GST base and starting with the treatment of food. See *Committee Hansard*, Canberra, 14 June 2017, p. 8. For Australia’s future taxation system (AFTS) review see discussion below and footnote 94.

⁴⁰ Mr Highfield, Private Capacity, *Committee Hansard*, Canberra, 14 June 2017, p. 4.

⁴¹ Mr Pier Parisi, *Submission 21*, p. 1.

⁴² ECU Australia, *Submission 22*, p. 1.

⁴³ Mr Pawson, The Tax Institute, *Committee Hansard*, Canberra, 6 September 2017, p. 5.

⁴⁴ Preliminary material in this report.

tax and BAS agents over the period.⁴⁵ The ATO website highlights the important role tax practitioners play in the tax system:

In Australia, tax professionals have a critical role in the tax and superannuation systems. They are intermediaries, conduits and influencers of behaviour, providing expert advice to clients to meet their obligations.⁴⁶

3.40 Also noting why Australians employ a tax professional to help them meet their taxation and superannuation obligations, the ATO states:

They choose to do so for a variety of reasons including time, complexity and the peace of mind of having a professional managing their affairs. Many agents provide holistic, value-added services that support their clients to succeed; often preparation of taxation forms is only a minor part of their overall service.⁴⁷

3.41 The Australian tax system supports the use of taxation intermediaries as it provides taxpayers with a deduction for the cost of managing tax affairs (irrespective of complexity). The Committee heard evidence that this was inefficient, and that the calibration of the tax system towards overpayment of taxes with refunds provided for workplace deductions, for example, is fuelling a costly 'refund churn' while supporting late lodgement and late payment of tax obligations.⁴⁸ The increased capacity for fraudulent activity with refunded tax overpaid was also highlighted:

My particular focus is on the personal income tax. You have millions and millions of taxpayers where the average refund is something in the order of \$3 000 across all individual taxpayers. You have a huge traffic of refunds. It is very easy to conceal fraudulent refunds in a mass traffic of high-value refunds.⁴⁹

3.42 The ATO advised that 74 per cent of all tax entities (individuals and businesses) employ a tax professional to help them comply with their

⁴⁵ ATO Annual Report 2016–17, p. 4. Included in the definition of tax practitioners are lawyers and consultants.

⁴⁶ ATO, 'Working with Tax Professionals' <www.ato.gov.au/About-ATO/About-us/In-detail/Key-documents/Working-with-the-tax-profession/> viewed 15 March 2018.

⁴⁷ ATO, 'Working with Tax Professionals', viewed 15 March 2018.

⁴⁸ Mr Richard Highfield, *Submission 6*, pp. 11–14.

⁴⁹ Mr Highfield, *Committee Hansard*, 14 June 2017, p. 3.

obligations.⁵⁰ It is notable that only five per cent of small businesses do not use an agent for their annual return.⁵¹ Many small businesses also employ BAS agents to assist with their PAYG and GST obligations. The ATO emphasises that:

This means that tax practitioners—tax and BAS agents, accountants, lawyers and advisers—have a key role in influencing taxpayer engagement with the system.⁵²

- 3.43 There was speculation that the very high use of tax professionals by Australian taxpayers (even with basic tax affairs) is indicative of the perceptions of a complicated tax system, and fear of being penalised for making an error or omission. A continuing high level use of tax professionals by individuals despite easier and more efficient self-serve tax return mechanisms online may also reflect access and security concerns. Either way, tax professionals are an integral support to the architecture of Australia's tax system.

'A majority' of taxpayers comply

- 3.44 Despite the intricacies of the Australian tax system in many areas, and the continuing high use of tax agents for (even simple) tax and reporting obligations, the ATO has advised:

Australia is fortunate to have a healthy tax system with high levels of voluntary compliance. Our tax system works on a self-assessment basis, and the vast majority of Australians and businesses do the right thing by meeting their obligations under the law without the need for intervention from the Australian Taxation Office (ATO). Most taxpayers respond well to help and support and the majority lodge and pay their tax on time (or soon after the due date) with over 95 per cent paid within 90 days.⁵³

- 3.45 Australia has had a self-assessment tax system since 1986–87.⁵⁴ Under this system, willing compliance rests on some basic assumptions about

⁵⁰ ATO, *Submission 15*, p. 3.

⁵¹ ATO, *Submission 15*, p. 3.

⁵² ATO, *Submission 15*, p. 3.

⁵³ ATO, *Submission 15*, p. 13.

⁵⁴ Explanatory Memorandum to the Tax and superannuation Laws Amendment (2015 Measures No. 5) Bill 2015, *Chapter 4, Third Party Reporting*, p. 59.

Australians' perception of the tax system, its role in raising revenue for government, and the ATO's integrity as its administrator.⁵⁵ The ATO's 2016-2017 Annual report states:

Our approach is based on the belief that Australians value the tax and superannuation systems as an essential part of effective government. They know that fair and efficient tax and superannuation systems, based on self-assessment, depend on people's willingness to participate. Willingness to participate is driven by community perceptions of the integrity and complexity of the tax and superannuation systems and of the ATO's integrity and professionalism.⁵⁶

3.46 The ATO assesses tax participation using four key indicators for each of its client groups:

- correctly registering in the tax and superannuation systems;
- lodging tax information on time;
- reporting complete and accurate information; and
- paying tax obligations on time.⁵⁷

3.47 The Tax Commissioner Mr Chris Jordan AO listed the factors that support taxpayer engagement:

How and how well taxpayers engage with the tax system is dependent on a number of factors, such as: the complexity or degree of difficulty, and, conversely the ease of compliance; perception of fairness of the system; social and cultural norms; financial pressures; broader economic conditions; the tax practitioners they use and others who influence people's behaviour; importantly, confidence that others are doing the right thing in the system, and, if not, are being appropriately pursued by the ATO; and the quality of the experience people have when interacting with the ATO. These are all the sorts of things that drive engagement with the tax system.⁵⁸

⁵⁵ Information in this section from Australian Taxation Office (ATO), *Commissioner of Taxation's Annual Report 2016–17*, October 2017 [here after ATO Annual Report 2016–17], p. 12.

⁵⁶ Information in this section from Australian Taxation Office (ATO), *Commissioner of Taxation's Annual Report 2016–17* [here after ATO Annual Report 2016–17], p. 12.

⁵⁷ Information in this section from Australian Taxation Office (ATO), *Commissioner of Taxation's Annual Report 2016–17* [here after ATO Annual Report 2016–17], p. 12.

⁵⁸ Mr Chris Jordan AO, Commissioner of Taxation, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 1.

- 3.48 The ATO 2016–17 annual report provides information on compliance by sector. As previously noted, individuals represent the largest segment of Australia’s registered taxpayers—over 10.9 million people, the majority of whom lodge and pay their taxes on time.⁵⁹
- 3.49 Small business (classified as those businesses with annual turnover of less than \$2 million) is the next largest group—comprising 3.8 million businesses. According to the ATO, over 2016–17, 70 percent of small business paid on time, with some sectors, for example, the construction sector, lagging considerably behind.⁶⁰

Engagement by design

- 3.50 Australia’s taxation administration system is being reinvented under tandem commitments made within the ATO Program Blue Print and under the Government’s Digital Transformation agenda.⁶¹
- 3.51 The objective of this system redesign is to reduce the time it takes to comply with the tax and superannuation system and, for businesses, to ensure tax engagement activities dovetail with the natural systems in operation within businesses. This serves the dual purpose of simplification of required regulatory activity and reducing time taken to comply.⁶² In addition, the reinvention aims for improved tax system transparency on the monitoring of and dealing with non-compliance in the system.
- 3.52 The Tax Commissioner advised:

Our intention is to make [tax] engagement easier, painless and infrequent for both taxpayers and their practitioners. We want a design for the majority of people who simply want to do the right thing. We want to lighten their load—especially for those who are low-risk, transparent with us, and have more straightforward affairs. Things like pre-filling data in tax returns, the myDeductions function in our app, and myTax itself on myGov are good examples of our services that do this.⁶³

⁵⁹ ATO Annual Report 2016–17, p. 12; ATO, *Submission 15*, p.12.

⁶⁰ ATO Annual Report 2016–17, p. 12.

⁶¹ ATO, *Submission 15*, Appendix 2, *ATO Digital Strategy*, December 2016, p. 2.

⁶² Compliance costs of meeting tax system obligations are discussed further in Chapter 4.

⁶³ Mr Jordan AO, ATO, *Committee Hansard*, Canberra, 29 March 2017, pp. 1–2.

3.53 Mr Neil Olesen, Second Commissioner, Client Engagement, explained this involves re-designing systems to meet client needs at the front end of the process, rather than focussing on end compliance:

Increasingly, our approach not only with small businesses but across the markets is to engage early with them and try and give people the tools and ability to serve themselves well, rather than a down-the-track, ‘Oh, you got it wrong—ha, ha, caught you.’ Rather than that model, we are trying to do things upstream in real time and get people on the right track, because all our experience tells us that getting people on the right track early and giving them the tools that make it easy for them to meet their obligations is a far more productive way, in the long run, to run an effective tax system.⁶⁴

3.54 Under the reinvention program the ATO has various projects underway which support this approach, along with a broad ethos of integrating ease of use and reducing compliance time for taxpayers in all tax system interactions.

3.55 Business software packages have been devised which allow reporting of information and payments to the ATO in a less intrusive manner, avoiding duplication. This has been possible through a collaborative approach undertaken between the ATO and software providers as will be discussed later in this chapter. Further enhancements to such systems are possible by triggering reporting during the natural flow of business activity.

Mr Peter Strong, Chief Executive Officer of the Council of Small Business of Australia (COSBOA) emphasised the value in this to small business operators:

I’m doing a pay run anyway. Why do I then have to do a GST or a PAYG? That’s the sort of process that we’re looking at: seamless and the complexity is covered within the system. I don’t see it; I’m happy; it’s done; I can go back to business.⁶⁵

3.56 The ATO has been working with the software development industry to enable the design of seamless business and reporting systems such that taxpayers can procure suitable software to support business activities and accounting systems but which also facilitate reporting and in some cases,

⁶⁴ Mr Neil Olesen, Second Commissioner, Client Engagement, ATO, *Committee Hansard*, Canberra, 29 March 2017, p.6.

⁶⁵ Mr Peter Strong, Chief Executive Officer, Council of Small Business of Australia (COSBOA), *Committee Hansard*, Canberra, 16 August 2017, p. 2.

payments⁶⁶ to the ATO.⁶⁷ Mr John Dardo, the ATO's Deputy Commissioner, Digital Delivery and Chief Digital Officer, identified four foundation principles supporting this model for robust digitised tax system interaction:

The first thing is the standards...what are the standards that are consumable by everyone and agreed by everyone. That is one.

The second one is the interfaces. What are the interfaces that are available from the bodies, the accounting software, the payment providers, the banks or the new payments platform? What are those interfaces and the overlay services sitting on top of the payments platform, for example, that can be used or reused to do exactly what you described?

The third thing is that at a government or a regulatory level, you may not have to mandate it. If a software provider chooses to do that with a payment provider, be it a bank or somebody else or with the platform itself, that is cool.

The last thing is the attitude of society in terms of getting there or wanting it or needing it or asking for it. We will see an evolution to that. The question is when and how fast. ⁶⁸

3.57 Mr Dardo's last point highlights the tailoring of software which is possible under this model. And more tailored systems mean more user-friendly and efficient systems which foster willing participation. Such systems relate to the reduction in time and effort to deal with red tape which means that non-compliance is less likely.

Consultation process

3.58 The ATO has developed a strong consultation model with a Consultation Steering Group overseeing formal arrangements. The agency has nine stewardship groups with diverse representation to enhance engagement with different client groups including tax practitioners, small business, the superannuation industry and others with a role in the tax and superannuation systems.⁶⁹ In addition, the ATO is consulting 'in the field'.

⁶⁶ For example, 'Single Touch Payroll' systems enable reporting to the ATO at the time a payroll is run.

⁶⁷ The ATO supplies application programming interfaces (APIs) to developers so that business specific software can be developed to also integrate tax reporting requirements.

⁶⁸ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 21.

⁶⁹ ATO, Commissioner of Taxation Annual Report 2016–17, p. 128.

The ATO's Acting Deputy Commissioner for Small Business

Ms Emma Rosenzweig outlined the approach:

We have a key stewardship group that has some peak body representatives and some key industry representatives. That is one mechanism that we use to get feedback from them. We are actually out talking to small businesses an awful lot. The commissioner talked about people asking to be shown products more. We have had a very deliberate program over the last eight or nine months where we are contacting new small businesses and offering to come out and show them a lot of the services and new tools that we have to help them.

We have also developed a program with the department of industry about being new to business. For any business that registers for an ABN and gives us their email address, we have a program of emails that go out in the course of the year. Rather than swamp them with a big pile of booklets when they start, they get some just-in-time information throughout the year about their obligations, particularly in that first year, to try and help them get off on the right foot.⁷⁰

- 3.59 She additionally noted that community consultation and outreach is a very constructive way to embed a compliance framework, and particularly helpful for new businesses:

Those new businesses get invited to tax essentials seminars in the first couple of months after they have started. Through that, we are able to talk to a lot of them about what they struggle with, where they find things challenging, and make sure that they have as much information and support as they need. So we are out there really talking to businesses an awful lot.⁷¹

- 3.60 As Chief Digital Officer Mr Dardo advised of current consultation over development of minimum standards to ensure software developers are designing systems that are cyber-safe for businesses and secure for integration into ATO systems. Recent investment was in the development of a certification or register system, to ensure software developer or mobile app providers connected securely with core ATO systems, and that secure authentication is at the front of their systems; to vet identity and ensure secure access.⁷²

⁷⁰ Ms Emma Rosenzweig, Acting Deputy Commissioner, Small Business, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 6.

⁷¹ Ms Rosenzweig, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 6.

⁷² Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 18.

- 3.61 He also emphasised that consultation over an operational framework for the ATO's digital 'eco-system' would be ongoing, with five key focus areas identified. It was expected that the minimum standards for the framework would be agreed by software developers, banks and superfunds in early to mid-2018 for implementation the following year.⁷³
- 3.62 Further elements of the cyber-safe framework are outlined in Chapter 6, 'Challenges and Solutions'.
- 3.63 A discussion on the ATO's partnership with software developers and stakeholders for system design and implementation follows.

Compatible lodgement platforms and products

- 3.64 The ATO is responsible for administration of taxation services and activities, but does not carry responsibility for policy design and review. Without broader jurisdiction over tax system reform and streamlining, the ATO has focused on delivery of systems and services to address identified problems. As Commissioner Jordan explained: 'Our intention is to make this engagement easier, painless and infrequent for both taxpayers and their practitioners'.⁷⁴
- 3.65 Accordingly, technical solutions such as pre-filing, myTax, the individual and sole trader deductions app tool (myDeductions) and integrated software solutions for business like Single Touch Payroll systems (using Standard Business Reporting – SBR principles⁷⁵) are being progressively evolved to improve ease and transparency. This process is part of the ATO's work with software developers to finesse products and services so that responses are tied to the 'natural systems' used by taxpayers, and consequentially will involve a process of continuous conversation between stakeholders in the tax eco-system.⁷⁶

⁷³ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 19.

⁷⁴ Mr Jordan AO, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 1.

⁷⁵ Standard Business Reporting (SBR) is a standard approach to online or digital record-keeping that was introduced by the Australian government in 2010 to simplify business reporting obligations. Software Developers (SWDs) build SBR rules into their business/accounting software to make it 'SBR-enabled'. Businesses that use SBR-enabled software can report using information already recorded as part of running their business. < www.sbr.gov.au/about-sbr/what-is-sbr > viewed 13 March 2018.

⁷⁶ Commissioner Claire O'Neill, ATO, 'Using Digital Delivery to Enhance the Integrity of Tax Systems', OECD, *Tax Administration 2017*, p. 166.

Software development and SBR

3.66 The ATO's Digital Strategy positions the agency as a facilitator of direct information with its clients—taxpayers, and with the third parties who hold their information:

Every connection within a digital eco-system is a flow of information and each part plays an important role in order for the ecosystem to function as a whole. Emerging and changing trends in technology will drive the evolution of our digital ecosystem—from the services we provide, the channels we make available, to the accessibility of these from current and future devices. Future success will be dependent on identifying the real needs of all clients (taxpayers and their representatives, including intermediaries), partners (eg government agencies, intermediaries, third party service providers) and staff.⁷⁷

3.67 The Strategy foresees flexible and customised modes of transferring information from taxpayers to the tax administrator via software which is customised to business needs—while at the same time meeting the data requirements of SBR.

3.68 The SBR was envisaged as is a whole-of-government business reporting standard which, through endorsement by the Council of Australian Governments (COAG) in 2008, was introduced in 2010. It was developed to have a single set of reporting definitions and eventually enable that information to be sent directly and electronically from business systems to participating government agencies. Compliance cost savings for business using SBR were predicted to reach \$800 million per year accruing from reporting to government dovetailing with 'natural systems'—those actions already being performed in the course of business operation.⁷⁸

3.69 The ATO Digital Strategy states:

Existing partners are expected to evolve their offerings to meet customer expectations and new digital solution providers will emerge with the ability to think and act differently. This will lead to services and functions being

⁷⁷ ATO, *Submission 15*, Appendix 2—ATO Digital Strategy, December 2016, p. 3.

⁷⁸ *Australia's Future Tax System—Report to the Treasurer*, G4. 'Client Experience of the Tax and Transfer System', pp. 712, 713.

delivered differently as innovative approaches disrupt and transform the ATO's traditional business model.⁷⁹

- 3.70 Small businesses can reap considerable rewards from this methodology because they carry a relatively greater cost of compliance burden than larger businesses. It also presents an opportunity for developers to produce customised interfaces for particular sectors starting with small scale business—but enabling 'scale up' possibilities.⁸⁰

The role of APIs

- 3.71 As discussed in Chapter 2, technical advances in the design and implementation of the 'end-to-end solutions' which service modern tax systems rely on the use of Application Programming Interfaces (APIs). An API provides software developers with key parameters so the Tax Office can glean required data from the information sent from taxpayers' software systems. These systems may be created with very specific client functionality but, in communicating via an ATO API, will be able to produce the data the ATO requires.
- 3.72 According to Deputy Commissioner Dardo, Australia is in advance of other nations in the development and sophistication of APIs, and also in their implementation.⁸¹ He cited the ATO's development of its SBR system as a case in point—

Our biggest investment in the IT space, our highest priority, is enabling standard business reporting. There is old world digital, which is portals type stuff. New world digital is machines talking to machines, so software. In that new world digital, what you must have is APIs, or application programming interfaces. If we go back a few years, in 2014, we only had 70 of them. We now have over 250 of them. A few years ago, we only had a small number of providers connected. We now have over 346 providers connected. Our biggest investments at the moment are how we turn those APIs into more resilient systems.⁸²

⁷⁹ Appendix 2, *ATO Digital Strategy*, December 2016, p. 4, in ATO, *Submission 15*.

⁸⁰ *Australia's Future Tax System—Report to the Treasurer*, G4. 'Client Experience of the Tax and Transfer System', p. 714.

⁸¹ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 22.

⁸² Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 22.

3.73 Mr Dardo noted that the critical areas of the ATO's digital IT focus are in dealing with the sheer scale of data available, the availability of the ATO to meet client needs, the investment in this area for both function and security, and the development and enforcement of good standards:

As we become more connected, people are depending on us to be available more than just 6.00 am to 6.00 pm. So how do we make them more resilient? How do we scale up? Last year, we did 12½ million interactions in one of the gateways. We will probably hit a billion next year. So it will be 10 billion the following year. We are talking scale, availability, investment, standards, technology and security. That is our biggest focus in the digital world. So we are absolutely up for the journey.⁸³

3.74 Mr Olesen explained how symbiosis with commercial applications was a key objective for the ATO in design of APIs:

Philosophically, we are committed to making services available for consumption into commercial software. As we make services available that we might choose to use ourselves and make available to the public ourselves, in parallel, we make the APIs available for software developers to consume and incorporate into their own products, because we understand that the commercial providers of software are probably the best people to innovate and integrate and provide good services to people. And, if they can access the services we want those people to have through the APIs that we make available, then that is a very good place for us to be. That is, in fact, our key direction—trying to make all the services that we have available for consumption and integration into software products.⁸⁴

3.75 Mr Matthew Prouse of accounting software platform specialist Xero Australia reported that there are approximately 70 software developers now working with the ATO in this collaborative space. He advised that even niche applications, such as those developed by the private sector for the childcare industry, are able to work in with the ATO's systems by utilising the SBR framework:

So a number of developers are creating software for businesses, taxpayers, tax agents and industry using that SBR framework. Seventy is a good number. It is a good starting point. There are some very large players in that space that employ hundreds of staff. We and MYOB are both appearing before this committee today. We sit in that space. There are some very small developers

⁸³ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 22.

⁸⁴ Mr Olesen, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 4.

as well that are working and developing quite innovative solutions for their specific niche. It might simply be, 'We develop software that completes one particular form that is really important for a particular industry'.⁸⁵

Partnership, not competition

3.76 The Tax Office's Reinvention program recognises that to gain the desired experience for taxpayers, the ATO will have to work closely with software developers. The ATO's Digital Strategy, December 2016, also states this clearly, anticipating that fulfilment of tax and super obligations will form an integral part of taxpayers' core business processes, and based on the ATO's robust collaboration model with software developers.⁸⁶ The strategy also stipulates that:

All services and interactions will be digital and utilise SBR-enabled technology and infrastructure. This will enable businesses and tax practitioners to connect with the ATO and across government.⁸⁷

3.77 Mr Timothy Reed, Chief Executive Officer of MYOB Australia, endorsed the ATO's development of tax platforms and digital tools in collaboration with industry:

Let me start by saying that I think the ATO blueprint is absolutely headed in the right direction—that they are building a digital platform and they are opening APIs to connect to providers such as MYOB and our competitors. So I think that is the right direction. I empathise with the challenge that they have; they have a bus that is moving down the highway and they have to try and refit it and retrofit it as it moves, and that is never an easy thing. But there is no doubt that at times the change and the rollout of that change creates a challenge for us and for others in the industry.⁸⁸

3.78 Mr Prouse emphasised that the ATO is seen as a partner and not a competitor with the private sector in meeting these development challenges:

As a software developer, we do not see the ATO as a competitor. Fundamentally, the ATO is our partner. They are the wholesale provider of a lot of the services and infrastructure that we are reliant upon to deliver services for small business. Historically, if you think about it, the ATO has

⁸⁵ Mr Matthew Prouse, Xero Australia Pty Ltd, *Committee Hansard*, 27 October 2017, p. 4.

⁸⁶ ATO, *Submission 15*, Appendix 2, *ATO Digital Strategy*, December 2016, p. 7.

⁸⁷ *ATO Digital Strategy, Future Experiences*, December 2016, p.7.

⁸⁸ Mr Timothy Reed, MYOB Australia Pty Ltd, *Committee Hansard*, 27 October 2017, p. 12.

always provided stationery and, effectively, a safety net of services and functionality for individual taxpayers and businesses. I go and choose to employ someone in my small business and my employee needs to complete a tax file number declaration form. — I would not say the ATO is competing with us there. It is the same for things like business activity statements. There are requirements for individuals or taxpayers to have access.⁸⁹

3.79 Mr Prouse did, however, ask for the Government's commitment to evolution of reliable platforms and products around which the private sector can continue to innovate solutions, saying:

We recognise that the ATO has taken significant steps, but the needs of Australian small business threaten to outpace the technical capabilities of some of these government agencies. As paradoxical as it sounds, technology presents an opportunity to humanise the bureaucracy. It can provide taxpayers with real-time access to government information and assistance. The creation of APIs and deeper connections to business software like Xero can lead to 24/7 accessibility anywhere, any time on any device. Business owners ultimately want a tax system that is as simple, safe and user friendly as internet banking. For Australian small business to have confidence to grow, they need certainty about government platforms and policies. We urge policymakers to continue their efforts to make tax digital here in Australia and embrace cloud technology. We at Xero stand ready to partner with you in this endeavour.⁹⁰

3.80 At hearings, Deputy Commissioner John Dardo reiterated the conviction that the partnership model is crucial to the ATO's future vision. He cited the ATO's shift in focus from portal delivery to enabling products using SBR which are designed to connect with the accounting products that taxpayers use, not duplicate them:

For businesses, it will be a basic product. You can view and you can probably do some very basic things. We will never do payroll. We will not do your accounting systems. We will not do the complex stuff. It is a very basic view product. For tax agents, we currently have a product that is old. We will refresh it in the coming 12 months. But we are not going to try to compete with software developers in terms of the really awesome stuff that exists in the new practitioner lodgement system or practitioner enabled software. Over time—it might be a few years—even the agent portal will probably diminish

⁸⁹ Mr Prouse, Partner Solutions Manager, Xero Australia Pty Ltd, *Committee Hansard*, Canberra, 27 October 2017, p. 3.

⁹⁰ Mr Prouse, Xero Australia Pty Ltd, *Committee Hansard*, Canberra, 27 October 2017, pp. 1-2.

because they will be able to do it in their software once, not twice. — Our main game is enabling the natural system, not the portals for business and agents.⁹¹

Digitalisation and tax complexity

- 3.81 As noted, it is not the ATO's role to initiate wholesale tax reform, nor to address those aspects of the law that create complexity for tax administration. This is the Government's role and the Treasury is the responsible agency.⁹²
- 3.82 The most far reaching and recent review conducted for the Treasury into tax simplification was the inquiry in 2008-09 into Australia's future taxation system (AFTS), widely known as the Henry tax review.⁹³ During the inquiry there were calls for reconsideration of a number of recommendations made in the review report (May 2010).⁹⁴
- 3.83 Treasury's Mr Graeme Davies, Acting Division Head, Tax Framework Division, however, explained why Treasury took a very conservative stance on tax reform:

If we think about the tax system, it gets complex for a reason, and that reason is you start with a system and then you keep adding onto it, changing it, adjusting and reforming it. Almost every area of the tax system you look at has that as its characteristics. That is the original idea that was somewhere in the eighties, nineties or early 2000s, and we have since made a number of amendments in there. This is a gross generalisation, but — almost every time amendments like that happen — what is really hard to do when you are amending one part of the law is understanding what it does to the other parts

⁹¹ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, pp. 22–23.

⁹² Mr Jordan AO, Commissioner of Taxation, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 1.

⁹³ See *Australia's Future Taxation System*, Report to the Treasurer, December 2009, released May 2010 <taxreview.treasury.gov.au/content/Content.aspx?doc=html/pubs_reports.htm> viewed 13 March 2018.

⁹⁴ For example, Recommendation 11 for standardised workplace expense deductions, see The Tax Institute, *Submission 16*, p. 7; Mr Richard Highfield, *Committee Hansard*, Canberra, 14 June 2017, p. 1; and also for simplification of Personal Services Income (PSI) rules in response to the evolution of the sharing economy, see Mr Tony Greco, General Manager, Technical Policy, Institute of Public Accountants (IPA), *Committee Hansard*, Melbourne, 18 July 2017, pp. 3–4. Note that those recommendations not adopted relate to broader tax reform as opposed to recommendations under G4 on client engagement.

of the law. Those interactions get more and more complicated the more and more amendments that are in there.⁹⁵

- 3.84 In view of this, Commissioner Jordan listed the ATO's strategies to address the challenges for taxpayers in navigating a relatively complicated tax system:

I can see a number of key strategies that we will need to, or will continue to, pursue and deliver on—very much a service ethic in the ATO, helping to facilitate people through what is a complex system; a focus on prevention rather than correction; greater and more sophisticated use of data for both service and compliance—it is important to use that for a service element as well; increased use of behavioural insights to help us work more constructively and collaboratively with taxpayers to get the right outcomes; increased digital offerings; leverage our relationships with industry; greater collaboration with the tax profession to tackle matters jointly; and to drive significant cultural change in the Australian community to perhaps the way some people approach their obligations, particularly around the cash economy and some of those issues where it might be okay to cheat a bit on our tax returns in our deductions. A significant education campaign is required there.⁹⁶

- 3.85 The ATO's Chief Digital Officer Mr Dardo explained how well designed digital products can simplify the system for users, without changing the underpinning legislation: 'If you have data, you can actually simplify what you do with it or behind it or around it. In a digitised world, you actually are moving away from forms'.⁹⁷
- 3.86 Mr Dardo went on to emphasise that the ATO is thus 'not digitising the paper form' but 'thinking differently', highlighting significant progress with BAS, including, in 2017, the issuing of 'push returns':

A simplified BAS is an example. It has been simplified for particular segments. There are some options about how you do and do not report through the year for small businesses. So that exists. In a digital world, sometimes you can simplify just by hiding the complexity. You do not actually have to legislate for it or change it. You just hide it. This year, we had push returns. Push returns were available for a particular client segment where, based on

⁹⁵ Mr Graeme Davis, Acting Division Head, Tax Framework Division, the Treasury, *Committee Hansard*, 29 March 2017, p. 15.

⁹⁶ Mr Jordan AO, ATO, *Committee Hansard*, Canberra, 29 March 2017, pp. 1–2.

⁹⁷ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 25.

previous years, we knew they did not have complex affairs. We just said, “We think this is your position” and they just went, “Actually it is”.⁹⁸

- 3.87 Ms Rosenzweig, of the small business area in the ATO, referred to work on the old and new iterations of myTax and how the new version is considerably more customised for each client:

But if you compare the myTax product, for example, to the old Etax product, you find that it only asks you questions that are relevant to you. So it is not making you step through every possible question that an individual might have to answer. It does really tailor it down to the data that is relevant to you. I think in lots of ways, in seeking reporting from people, we are asking for the information and they do not have to fill out a checklist of “Did you have CGT [Capital Gains Tax]? Did you have this?” It is more about seeking the data that is relevant to them, which then hides all the complexity that is just not relevant.⁹⁹

- 3.88 Mr Andrew Watson from the Tax Practitioner Digital Service area of the ATO spoke about further advances, in which the data is the locus of function rather than form filling per se. He cited the Single Touch Payroll as a good example of this:

... the concept is around how that data helps a citizen fulfil their obligations under the tax law. Consider some of those obligations under the law. Income tax rates are based on net income over a 12-month period versus the GST, where we have obligations on a monthly and quarterly basis but the rate is still the same. Those obligations can be met in different ways. From a design point of view, the differentiation of forms and data is often spoken about. So the concept is around how the data meets the obligations. I think single touch payroll is a really good example of our first step on that journey of people meeting obligations through data. It just takes forms out of the equation. At some point, though, it is a policy thing about how the data lets you meet your obligations as a citizen under the provisions as they exist. A lot of them were designed around a form filling culture.¹⁰⁰

⁹⁸ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 24.

⁹⁹ Ms Rosenzweig, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 25.

¹⁰⁰ Mr Andrew Watson, Assistant Commissioner, Tax Practitioner Digital Service, ATO, Canberra, *Committee Hansard*, 27 October 2017, p. 25.

Tax systems and services

3.89 The ATO commitments to taxpayers under the Government's Digital by Default policy are extensive:

- **Individuals**— For those who choose to prepare their own return, myTax will continue to evolve to provide streamlined pre-filled assessments, expanding to a 'push' tax return for certain taxpayers, eliminating their need for lodgement. As more comprehensive data on individuals' income and deductions is captured in real-time, the option to develop a progressive variable tax withholding rate will be explored.
- **Business owners**— will have a streamlined registration process and access to a secure whole-of-government account with a digital mailbox and a 'tell us once' feature (as individuals already do with myGov). Business owners will be able to access contemporary, digital services from any device and manage third party authorisations at a whole-of-government level. Businesses will transition to event-based reporting to government, which will be automated via integration with their natural systems (eg via software).
- **Super funds**— will be able to use new digital services so that more of their obligations can be managed electronically. By delivering integrated services (eg via SBR-enabled software), the timeliness of processing rollovers and contributions will be increased, with data for employees, employers and funds improved through real-time validation.
- **Tax practitioners**— Tax practitioners fulfil a critical role in the tax and super systems. We will provide products and services that will integrate with their systems and make more data available to allow them to be more productive. Cloud authorisation and SBR-enabled practice management software will enable tax practitioners to work anytime, anywhere in a cloud-based or hosted solution. We are improving the ability for tax practitioners to authorise their staff to provide services to clients on their behalf.
- **Software developers**— We will work closely with developers to implement solutions that make fulfilling tax and super obligations easy for users and a part of core business activities. All services and interactions will be digital and utilise SBR-enabled technology and infrastructure. This will enable businesses and tax practitioners to connect with the ATO and across government.¹⁰¹

¹⁰¹ ATO Submission 15, Appendix 2, *ATO Digital Strategy*, December 2016, p. 7.

- 3.90 In progressing this agenda, the ATO has prioritised innovation in provision of key platforms and services for individuals and sole traders, including the ‘myTax’ system, data pre-filling and, more recently, refinements to the myDeductions app tool and the Contractor Assessment Tool.
- 3.91 Similarly, for small business, the Single Touch Payroll system is listed by the Digital Transformation Agency as a key government platform in its Digital Transformation Agenda—providing streamlined business activity and reporting functions and, potentially, greatly reduced compliance costs. The Single Touch Payroll is possible because of the SBR framework, as discussed previously.
- 3.92 The features of these key platforms or services are discussed in evidence as follows.

myTax

- 3.93 The internet-based myTax system, accessed through the myGov ‘portal’, replaced the e-Tax lodgement model from 1 July 2016. It has resulted in significant benefits to individuals and, more recently to sole traders, who now have access to more pre-filled data and a faster and simpler service. As the service is internet based it doesn’t require downloads and can be accessed from a range of internet enabled devices.¹⁰² As at January 2017, just prior to the ATO’s first submission to the inquiry, myTax had been used to lodge over 3.2 million tax returns.¹⁰³
- 3.94 The ATO has espoused the benefits of myTax pre-filling to taxpayers:
- myTax pre-fills tax returns with information reported by third parties such as financial institutions and employers. Pre-filling also enables the identification of lost or forgotten records and accounts, such as lost bank statements and payment summaries sent to previous addresses. This minimises omitted or incorrectly reported income and other errors for individuals and has been received very positively by the community.¹⁰⁴
- 3.95 Mr Olesen stated that while the costs of myTax are relative to those for the paper-based system, there are real advantages for the individual taxpayer in digital self-assessment:

¹⁰² ATO, *Submission 15*, p. 8.

¹⁰³ ATO, *Submission 15*, p. 8.

¹⁰⁴ ATO, *Submission 15*, p. 8.

Under paper returns, we had the same costs, so in a sense I think you are looking for the relative cost. I think the other thing to look for is the benefits. The amount of feedback we have had from people who do their own returns about the speed and ease of completing an online tax return has just been phenomenal. Frankly, I have genuinely been really surprised by how good that has been. For your average citizen, I think they have gone from an average tax return preparation time just with the old e-tax model, let alone a paper one, of about three-quarters of an hour. The average preparation time under myTax is more than halved—I think around the 15-to-20-minute range, from memory. There are some phenomenal benefits there, including speed of refund as well.¹⁰⁵

- 3.96 The ATO reports that: ‘Over five million individual clients and sole traders have a myGov account linked to the ATO’, with the main myGov platform used to disseminate tax system correspondence, including notices of assessment or statements of account.¹⁰⁶ Since October 2016 the myTax service has featured the ability to access a web chat service when using myTax—an interactive help service called ‘Alex’—and the unique ability to share a myTax screen whilst discussing a matter on the telephone with ATO staff.¹⁰⁷
- 3.97 The introduction of a web chat service was recommended by the Inspector-General of Taxation, along with voice recognition authorisation. In the 2015 review into services and support for tax practitioners, the Inspector-General had recommended that the ATO increase use of such modern modes of communication, in particular in ‘...developing a “web chat functionality”, to provide tax practitioners with useful information’.¹⁰⁸ Other services for tax practitioners are discussed later in this chapter.

Pre-filling

- 3.98 Part of the improvement in myTax could be attributed to pre-filling. Pre-filling is a service the ATO has offered since 2007, originally through eTax, to assist taxpayers finalise their tax returns.

¹⁰⁵ Mr Olesen, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 7.

¹⁰⁶ ATO, *Submission 15*, p. 8.

¹⁰⁷ ATO, *Submission 15*, p. 9.

¹⁰⁸ IGT, *Submission 5*, pp. 31–32.

- 3.99 The Inspector-General of Taxation’s submission noted the OECD view (2011) that timely data provision is important for the utility of pre-filing.¹⁰⁹ The Inspector’s 2013 review of data matching also indicated that lack of timeliness in submitting pre-filled data is an obstacle to early lodgement. The need for improved comprehensiveness, availability, and reliability of data was also raised.¹¹⁰
- 3.100 The introduction of formal third party data reporting regimes potentially reduces compliance costs to individual taxpayers and significantly:
- It also has the ability to be an effective compliance response to deal with some taxpayers omitting or underreporting income.¹¹¹
- 3.101 Input to the Inspector’s 2017 work plan process suggested the ATO could do more to assist taxpayers by collecting more data. However, the Inspector-General considered that targeting effective areas for matching and ensuring potential providers were technically enabled with ‘natural systems’ would be more important.¹¹² In addition, the ATO now receives much expanded ‘as-of-right’ third party data under the *Taxation Administration Act 1953* (TAA 1953) as a result of changes introduced progressively from 1 July 2016–1 July 2017 and stemming from the Tax and Superannuation Laws Amendment Bill (2015 Measures No. 5) Bill 2015.
- 3.102 The Tax Act now requires third parties to report on government grants; consideration for government services; transfers of real property; transfers of shares and units in unit trusts, and business transactions made through payment systems. This is in addition to the pre-existing third party data received which already included:
- Wage and salary data from employees;
 - Government welfare payments from Centrelink and other providers;
 - Interest income from financial institutions; dividend income from share registries; and

¹⁰⁹ OECD, *Tax Repayments: Maintaining the Balance between Refund Service Delivery, Compliance and Integrity*, 2011, p. 9.

¹¹⁰ IGT, *Review into the Australian Taxation Office’s Compliance Approach to Individual Taxpayers – Use of Data Matching*, 2014, IGT *Observations*, paras 2.29–2.34.

¹¹¹ *Explanatory Memorandum to: Tax and Superannuation Laws Amendment Bill (2015 Measures No. 5) Bill 2015*, p. 60.

¹¹² IGT, *Submission 5*, pp. 25–26.

- Medicare levy surcharge and private health insurance policy details from private health insurers.¹¹³

3.103 This is clearly a powerful source of information for tax compliance inducement and enforcement, depending on how the data can be currently utilised by the tax administrator. The pre-fill function can now provide sufficient information to completely pre-fill many individuals' tax returns.

3.104 At hearings, Professor Michael Hiscox, (then) Director of the Behavioural Economics Team of the Australian Government (BETA) suggested that the ease offered by software developments such as pre-filling supports voluntary compliance:

To the extent that the technology enables a lot of those interactions to be easier and simpler for people, compliance becomes much easier because all of that data is available and fed into the system so that the delivery of the service is actually better, simpler and easier for people. We expect it to have positive effects and to encourage more compliance because it is the easiest thing to do. You would have to do more to stay outside the system, or it would be more costly for you in terms of time and resources.¹¹⁴

3.105 Professor Robert Slonim, a professor of economics with 20 years of behavioural economics expertise and the Head of BETA since July 2017, highlighted the important moral nuance of individuals having to change correctly presented information to incorrect information to gain an advantage, rather than filling out incorrect information themselves. He said:

What I would argue is that if people were to want to actively provide false information, repopulating it makes it more difficult because they have to change it and actively go and take something that has been provided that is truthful.¹¹⁵

3.106 Professor Slonin thus indicated that a moral 'nudge' may also work where people are asked to 'sign off' on the accuracy of inaccurately pre-filled information (where it is to their advantage). A Committee Member made the point that pre-filling is not always accurate—'I think I earned \$5 000 last

¹¹³ Explanatory Memorandum to: Tax and Superannuation Laws Amendment Bill (2015 Measures No. 5) Bill 2015, p.60.

¹¹⁴ Professor Michael Hiscox, (now former) Director, Behavioural Economics Team (BETA) of the Australian Government, Department of the Prime Minister and Cabinet, *Committee Hansard*, Canberra, 10 May 2018, p. 12.

¹¹⁵ Professor Robert Slonin, Private Capacity, *Committee Hansard*, Sydney, 17 July 2017, p. 30.

year, according to the ATO. It was not quite right. It was just as well I did not accept it'.¹¹⁶

- 3.107 Second Commissioner Olesen made the important distinction between what taxpayers can now view—for individuals and small business—and what the ATO can view:

...originally, when we got that data—going back to 10 or 15 years ago—it was for us to see, after the event, whether you had returned all of your income. With new technology and the earlier availability of the information, increasingly now what we do is make available to you what we know so that that helps you fill in your tax return.¹¹⁷

- 3.108 Further discussion on pre-filling appears in Chapter 4, in regard to compliance cost reduction and the likely impact on use of tax agents for simple tax returns.

Deduction and contractor assessment tools

Mydeductions tool

- 3.109 The Commissioner of Taxation mentioned in testimony the ease and convenience of pre-filled data for taxpayers completing digitised returns. He indicated, however, that even though a 'push return' was a near-future possibility in this area,¹¹⁸ the desire of taxpayers to claim a deduction remains a hurdle. Given that individual deductions may be claimed by taxpayers under the Tax Act, and that the proportion of claims by individual taxpayers is so high, a deductions processing tool, the myDeductions app has been developed by the ATO for use with myTax.
- 3.110 The Commissioner explained how this app streamlines the claims process for taxpayers and enables a repository of claim supporting evidence:

With the app I mentioned, myDeductions, if you have a bit of bank interest and you earn a salary or wage...when you make a donation you can take a photo of the receipt, put it in under the drop-down menu 'Donations' and it is done, by Briefcase or something. If it is under \$300, I think you can deduct it straightaway. It is 100 per cent business use, of course. You can put that in

¹¹⁶ Ms Julie Owens MP, *Committee Hansard*, Canberra, 27 October 2017, p. 4.

¹¹⁷ Mr Olesen, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 2.

¹¹⁸ As noted above, a push return is essentially a pre-filled statement of tax activity for a taxpayer to approve as correct.

‘Work related expense’ and it uploads directly to the right labels in your tax return. So, if you just have a few deductions or donations during the year, and all your income side is done, it is uploaded, literally, and you can look at it all.¹¹⁹

3.111 He elaborated:

For sole traders in business, it is pretty much the same. We have a simplified version for them. On the go, between jobs, they can input their income and their deductions, and it is all uploaded. Now, that is only for sole traders, like an individual who might be a tradie or something like that, or a consultant doing some work. It is all done. It is all there for them. Quarterly instalments can come in and you can vary them, all on your smart device.¹²⁰

3.112 However, ETax Accountants considered that the ATO ‘has unnecessarily gone further to invest in the development and operation of more complex tools and services, including mobile apps for recording deductions, which were pre-existing offerings available elsewhere at low or no cost to consumers.’¹²¹ The submission recommended that:

The ATO should not behave as a taxpayer-funded competitor against free-market Australian businesses, including against tax agents, and should not seek to copy, duplicate or challenge commercially available services without clear, early-stage and public justification and evaluation including transparently addressing costs and contestability.¹²²

3.113 This view contrasts with the fact that the cost of hiring a professional tax agent to complete a tax return is a taxpayer-funded cost through the allowable deduction for management of tax affairs.

3.114 There was also concern from some participants that the online tools could prompt individuals to start making claims they had not been able to make in the past. The Chartered Accountants Australia and New Zealand (CAANZ) commented:

...there is this sense that in an online, do-it-yourself world that you will, in your own mind at least, start to justify this thinking: ‘I am entitled to certain deductions. I have heard about claiming car expenses. I have heard about

¹¹⁹ Mr Jordan AO, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 3.

¹²⁰ Mr Jordan AO, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 3.

¹²¹ Recommendation 3, ETax Accountants, *Submission 7*, p. 5.

¹²² Recommendation 3, ETax Accountants, *Submission 7*, p. 5.

claiming laundry and uniforms.’ And on it goes. However, if they went to a tax agent—a good one—and the law was applied correctly, they would be told, ‘I’m sorry, that’s not deductible.’¹²³

3.115 There is a view, however, that the very high reliance on tax professionals to complete the tax returns of individuals with simple tax affairs is driven largely by the desire to claim deductions, particularly work-related expense deductions, or the concern taxpayers may miss out on the possibility of having a legitimate deduction. For example, Mr Highfield, an academic and tax expert, cited the high number of taxpayers with simple tax affairs who engage a tax professional and who claim work-related tax deductions:

Analysing records in the ATO’s Sample File, approximately 59 per cent of tax agent-prepared returns (representing around 5.6 million taxpayers) disclose income only from employment, pensions, and investments... just about all of the income of these taxpayers can be pre-filled by the ATO. Further examination of Sample File records reveals that for these taxpayers their deduction claims are concentrated on work-related expenses (81 per cent)...¹²⁴

Contactoressessment tool

3.116 The evolution of the gig (freelance worker) and sharing economies (where resources are ‘shared’ for a fee) have heightened the need to more clearly differentiate between the definition of contractors and employees. The evolution of this differentiation as a current tax system challenge is discussed further in Chapter 6.

3.117 The ATO provides guidance on how to determine whether a worker is an employee or a contractor.¹²⁵ Other countries have developed their own contractor assessment tools to help determine this distinction. Tax and Superannuation Australia, in a supplementary submission following appearance at a hearing in Melbourne, outlined how the UK’s HMRC contractor tool offered superior features as it posed in-depth, and more questions.¹²⁶

¹²³ Mr Michael Croker, Tax Leader Australia, Chartered Accountants Australia and New Zealand (CAANZ), *Committee Hansard*, Sydney, 17 July 2017, pp. 7–8.

¹²⁴ Mr Highfield, *Submission 6*, p. 8.

¹²⁵ ATO, *Difference between Employees and Contractors* <www.ato.gov.au/Business/Employee-or-contractor/Difference-between-employees-and-contractors/> viewed 12 March 2018.

¹²⁶ Tax and Super Australia, *Submission 12.1*, pp. 1–5.

3.118 There was some support in evidence for the review of Personal Services Income (PSI) rules in the Australian context to address potential inequities for employees who will miss out on workplace entitlements, such as superannuation, due to the contract-based nature of employment with big sharing companies like Uber. There was also the risk that taxpayers using the ATO's contractor tool would determine their status as a contractor given the significant tax concessions provided, or may inadvertently make errors. Notably, the ATO's website recommends obtaining a private ruling or independent advice in the case of uncertainty.¹²⁷

3.119 In regard to review of the PSI laws, Mr Tony Greco of the Institute of Public Accountants (IPA) referred to recommendations made in the 2010 Henry (AFTS) review report:

...the Henry review... picked up on this point, asking why we have a different tax outcome for the same activity. There are some fundamental policy issues there that I think need to be addressed, and I think they can't be ignored, given the fact that people can theoretically put themselves in the contractor space and avail themselves of all these tax concessions. And then you have someone very much in the same space being treated as an employee. So, I think there are some fundamental issues there. At the end of the day, if it mainly is a reward for personal effort, why do we have these differences in the tax treatment? So yes, we would like to see the PSI rules simplified.¹²⁸

3.120 Mr Greco elaborated his concerns about possible confusion and uncertainty for workers in this sector, who often lack tax literacy, as making the distinction is even difficult for 'seasoned professionals'. He noted:

The ATO, to their credit, have tried to introduce a contractor tool, where you answer a series of questions and it spits out a result, but the Tax Office will not stand by the result of that tool. If, according to that tool, you qualified as a contractor and subsequently you're found not to be a contractor, they're not going to stand by that. People don't have an ironclad way of ensuring they're on the right side of the line.¹²⁹

3.121 He also raised the significant potential impact of this uncertainty and room for mixed interpretation of the rules on the broader tax system:

¹²⁷ ATO, Contractors and Tools <www.ato.gov.au/Calculators-and-tools/Employee-or-contractor/> viewed 16 April 2018.

¹²⁸ Mr Tony Greco, General Manager, Technical Policy, Institute of Public Accountants (IPA), *Committee Hansard*, Melbourne, 18 July 2018, p. 4.

¹²⁹ Mr Greco, IPA, *Committee Hansard*, Melbourne, 18 July 2017, p. 3.

Given the risks involved in a significant number of people moving across into that contractor space under the existing rules, I think there is scope for simplification. But I think there has to be an acknowledgement that there's a revenue risk associated with a mass movement from PAYG to people in the contracting space... That shift into contracting space is only going to get bigger. So, we have advocated that the rules have to be simplified.¹³⁰

- 3.122 There was also discussion of improvements that could be made to the ATO's online contractor assessment tool, which by comparison with the United Kingdom's model is less comprehensive and accurate in its assessment of status.

Efficient products for business

- 3.123 The ATO has developed a suite of products to assist small business comply with broader tax obligations in easier and more efficient ways. The enabling platform for most accounting software products designed for small business to integrate with the tax and superannuation system is the SBR regime, as previously discussed. As at 21 December 2017 the taxonomy (dictionary) for government digital services commenced using SBR definitional taxonomy terms, with the Australian Reporting Dictionary phased out on 30 January 2018.¹³¹ SBR supports the potentially transformational business systems being rolled out by the ATO, including the Single Touch Payroll and SuperStream.

Single Touch Payroll

- 3.124 Single Touch Payroll (STP) systems provide a digitalised payroll process which is compliant with ATO requirements for data and payment transfer in a pay-run. Using STP is a mandatory requirement for employers with 20 or more employees from 1 July 2018. These businesses will be required to use an approved STP software package, to provide the payment information, withholding amounts and superannuation liability the day before each pay day, rather than the current annual reporting requirements. Along with the compliance benefits to the ATO of enabling this reporting information in a timely fashion, there are considerable benefits to business as Mr Dardo explained:

¹³⁰ Mr Greco, IPA, *Committee Hansard*, Melbourne, 18 July 2017, p. 3.

¹³¹ SBR, SBR Enabled Reports <www.sbr.gov.au/software-developers/sbr-enabled-reports> viewed 16 April 2018.

If you are doing payroll and you are doing it with paper or Excel and you move to a digital payroll system that is much more automated and much easier, particularly if you have more than two or three employees, you will notice a difference. So as software developers make more and better products available and as the law changes to say, 'Look, single touch payroll requires you to report payroll events every payroll event, not once a year on a payment summary', we will probably see a combination of the education, the service offering, the better product and the law shift requiring businesses to move...¹³²

3.125 Despite the expected benefits of the STP for businesses, some will require additional support to transition, as Mr Dardo explained:

For some businesses, there is more work that needs to be done to help them understand that spending three hours trying to format a spreadsheet or trying to keep a paper record and doing everything three times might not be as easy as actually moving to something that is a bit more digital. That is one. The second one is they might genuinely be not digitally literate.¹³³

3.126 Mr Dardo also contended, however, that as software providers develop more user-friendly interfaces that digital literacy or uptake will shift.¹³⁴

3.127 STP is anticipated to be mandatory for all businesses with 19 or fewer employees as of 1 July 2019—assuming the passing of legislative change.

E-invoicing

3.128 E-invoicing is a system which produces an invoice in an electronic format provided by the seller to the customer which follows a natural reporting system and avoids the duplication of record-keeping (and potentially also reporting) effort. An e-invoice can meet the requirements under the Tax Act for businesses to provide a tax invoice to customers providing the e-invoice contains the regulatory information required for a tax invoice.

3.129 One of the impediments to real-time, expedient e-invoicing is the ability to record the required information in the data transfer. Dr Anthony Richards, Head of Payments Policy, RBA outlined the data rich benefits which the New Payments Platform (NPP) offers. In terms of data contained in a transaction between parties and financial intermediaries in the NPP, he said:

¹³² Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 20.

¹³³ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 20.

¹³⁴ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 19.

It can contain anything. There will be just a lot more room for different fields in the message. You could have GST type information. You could have a hyperlink to a document. You could have a field that triggers an overlay service that kicks in. There are all sorts of things that are possible once you have a lot of data going with a payment rather than just 18 characters.

Currently, you cannot even put out your full name in those 18 characters.¹³⁵

3.130 COSBOA anticipates that e-invoicing will ‘expedite payments and also provide timesaving for businesses that will no longer need to type and retype invoices or use PDFs and the like to communicate B2B (business to business)’. E-invoicing also provides an opportunity for regulators to ‘reward those who use transparent and compliant accounting and sales systems’ by reducing compliance-related contact.¹³⁶

3.131 There are also likely to be efficiency benefits to small businesses in utilising e-invoicing over the alternative paper tax invoice, as Deputy Commissioner Rosenzweig explained:

There has been some research done—I think I probably have some figures—about potential savings per invoice going down from about \$30 an invoice to process a paper invoice down to about \$9 to process an electronic one. In addition, you can get paid faster. If the processing is faster, there is faster payment.¹³⁷

3.132 The ATO’s Chief Digital Officer Mr Dardo reasoned that e-invoicing will be a catalyst for greater digitisation of business systems:

‘If I’m doing e-invoicing, I might as well do the rest of it.’ The other lever will be increasingly as it becomes more normal for them to interact with others digitally, because others expect to be receiving stuff digitally or to be sending digitally, we may see the pressure of society actually starting to shift.¹³⁸

3.133 Mr Prouse of Xero Australia spoke about the progress of the development of e-invoicing standards in Australia:

So through the Digital Business Council, Xero has been participating in the development of e-invoicing. E-invoicing is an industry-wide standard. It is

¹³⁵ Dr Anthony Richards, Head of Payments Policy, Reserve Bank of Australia (RBA), *Committee Hansard*, 27 October 2017, p. 32.

¹³⁶ COSBOA, *Submission 25*, p. 2.

¹³⁷ Ms Rosenzweig, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 21.

¹³⁸ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 20.

involving software developers like Xero, payment providers, the banks and the ATO through the Digital Business Council. We recognise that e-invoicing is going to be a key part of the national business infrastructure for Australia.

The ATO's work around the invoicing is similar. The important thing about e-invoicing is getting the content of that invoice transferred from one business to another without any data entry. So I am not having to read a paper invoice and double-check that it is a 'three' and not an 'eight' or an 'eight', not a 'three' and manually enter that information. It is more than just exchanging pictures of invoices. It is about the data.¹³⁹

- 3.134 The Committee has noted that some jurisdictions overseas have mandated e-invoicing. However, the inquiry received no evidence supporting the need in the Australian context for mandating such services. Rather, if correctly designed at a system level, the benefits of such a service will be manifest and not require mandatory uptake as consumers will naturally take up such services.

SuperStream

- 3.135 Introduced in 2016, SuperStream is a mandatory system for employers to meet their superannuation contribution requirements. The system transmits funds and relevant information from employers to the employee's superannuation fund directly with data to the ATO linked to the payment by a unique payment reference number. The ATO receives the relevant information of these payments in a consistent format to help transfer the data directly into an employee's fund.¹⁴⁰
- 3.136 Mr Reed of MYOB Australia noted the compliance cost reductions for business resulting from the introduction of SuperStream:

SuperStream has materially reduced the amount of time it takes an employer to report super each quarter. I think the first client I spoke to who used our super compliant services said that it went from four hours to four minutes for her to do super on a quarterly basis. Those sorts of changes have come through...Everybody has to now report digitally. Regulation forced that change despite the fact that it was actually a big benefit to the business.¹⁴¹

¹³⁹ Mr Prouse, Partner Solutions Manager, Xero Australia Pty Ltd, *Committee Hansard*, Canberra, 27 October 2017, p. 1.

¹⁴⁰ ATO Annual Report 2016–17, p. 35.

¹⁴¹ Mr Timothy Reed, MYOB Australia, *Committee Hansard*, 27 October 2017, p. 14.

- 3.137 The ATO notes one significant benefit is the ability to use a single channel to pay multiple funds. The ATO's submission details that: 'It is expected to deliver savings to employers of approximately \$350 million per annum. Single Touch Payroll will further streamline and automate reporting obligations for employers through their regular payroll events'.¹⁴²
- 3.138 The ATO focuses on employers at high risk of not meeting their superannuation guarantee obligations for their employees.¹⁴³

The role of tax practitioners and intermediaries

- 3.139 In his 2015 review of the ATO's services and support for tax practitioners, the Inspector-General of Taxation concluded that taxpayer reliance on tax practitioners in Australia has gradually increased since the implementation of self-assessment (in 1986),¹⁴⁴ due to a number of factors, being:
- the complexity of the business operations and related regulations;
 - the individual taxpayers involvement in investment activities and income sources other than personal exertion;
 - the scope and complexity of tax law and related compliance; and
 - the use of the tax system to deliver social policies as well as to collect revenue.¹⁴⁵

High reliance on tax agents

- 3.140 As discussed in Chapter 2, although data assessments of tax agent usage may not be internationally comparable,¹⁴⁶ Australia is considered to have

¹⁴² ATO, *Submission 15*, p. 11.

¹⁴³ Currently, employers are required to make quarterly payments of 9.5 per cent of an employee's ordinary time earnings to a designated superannuation fund.

¹⁴⁴ IGT, *Submission 5*, p. 15. The Board of Taxation referred to statistics from the report: 'From only 20 per cent of individual taxpayers in 1980 to over 70 per cent of all individual taxpayers (8 million) and 90 per cent of all business taxpayers (2 million) in 2013–14', see *Submission 9*, p. [2].

¹⁴⁵ IGT, *The Australian Taxation Office's Services and Support for Tax Practitioners*, 2015, p. 2; <igt.gov.au/publications/reports-of-reviews/atos-services-and-support-for-tax-practitioners-2/chapter-1/> see also: ANAO, *The Australian Taxation Office's Management of its Relationship with Tax Practitioners*, 2002, p. 12, cited in IGT, *Submission 5*, pp. 15, 16.

¹⁴⁶ Mr Davis, Acting Division Head, Tax Framework Division of the Treasury alerted the Committee to the different uses of tax agents in various countries concluding that 'one of the challenges is looking at that data and asking: is that actually comparable?', *Committee Hansard*, Canberra, 29 March 2017, p. 14.

one of the highest levels of reliance on tax practitioners of any OECD country.¹⁴⁷ In 2015–16, the ATO reported that 74.2 per cent of all individuals and over 95 per cent of business taxpayers used the services of a tax practitioner.¹⁴⁸ The Taxation Commissioner stated that: ‘The 74 per cent figure is a blended thing; something like 90 per cent of businesses use an agent and something like...Sixty-eight per cent of non-business individuals.’¹⁴⁹

3.141 The Board of Taxation cited the Inspector-General’s 2015 report to observe:

... These current levels are among the highest in OECD countries, exceeding those of Canada (39 per cent), the United States of America (40 per cent), New Zealand (50 per cent) and the United Kingdom (67 per cent). This highlights that tax practitioners, in Australia, have even a greater level of influence on taxpayer compliance.¹⁵⁰

3.142 In relation to longer term trends in the use of tax agents, the ATO’s Mr Olesen confirmed that the introduction of self-assessment in 1986-87 had driven a spike in tax agent use, up from about 20 per cent in the 1980s. The Tax Commissioner considered that the size of the TaxPack had probably contributed to that rise, driving many people with simple tax affairs to a tax agent because it looked daunting.¹⁵¹ There were also other incentives to using an agent, such as the lodgement extension to May the following year and a tax agent’s expertise in taxpayer deductions.¹⁵²

3.143 In a supplementary submission, the ATO advised that: ‘Available data indicates a slow rise in the number of businesses using tax practitioners over recent years, while the number of individual taxpayers using a tax practitioner has remained steady at approximately 74 per cent’.¹⁵³

3.144 Mr Highfield, in testimony, reiterated evidence in his submission to the inquiry, that despite the ATO making much progress in the last decade with

¹⁴⁷ Mr Jordan, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 2.

¹⁴⁸ OECD, *Tax Administration 2015 Comparative Information on OECD and Other Advanced and Emerging Economies*, 2015, p. 267; cited in IGT, *Submission 5*, p. 16.

¹⁴⁹ ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 7.

¹⁵⁰ Cited in Board of Taxation, *Submission 9*, p. [2].

¹⁵¹ ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 8.

¹⁵² ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 8.

¹⁵³ ATO, *Submission 15.1*, [Answer to Question no.5], *Tax Practitioner Usage*, p. 5.

pre-filing, 'almost three-quarters of individual citizens use a tax agent'.¹⁵⁴ Hence, the high rate of tax agent use by individuals, he argued is—'simply to do with deductions'.¹⁵⁵

3.145 Deputy Commissioner Rosenzweig stated:

We are also conscious that small businesses really engage a lot through agents and intermediaries. A lot of our research shows that they go to an accountant as the primary source of their information and advice about the tax system.¹⁵⁶

3.146 The Tax Institute cited the 74.2 per cent figure to indicate the 'strong indication that taxpayers are heavily reliant on agents to meet their tax obligations. However, the submission noted that use of agents is not consistent across all taxes, nor all interactions with the ATO.'¹⁵⁷

New tax intermediaries

3.147 In addition to the traditional tax intermediaries noted above, there are increasingly new players providing services and products within the tax sphere. The Inspector-General's submission highlighted the emerging significance of software developers whose products are being developed to communicate directly with ATO systems, including SBR and STP enabled systems. The customer support from these new intermediaries, and associated costs, is also expected to transform the experience of taxpayers and their advisers in managing their tax affairs.¹⁵⁸

3.148 The Inspector-General's submission further observed that as the ATO continues to roll out technology supporting self-management of tax affairs, adoption of these systems by taxpayers will depend on there being 'ready access to adequate hardware, software and robust internet connections'. In this way, the broader sphere of software and hardware developers, along with telecommunications providers, will be important to service delivery.¹⁵⁹

3.149 The Taxation Practitioners Board reported that some of its members were concerned that the increased sophistication and automation of accounting

¹⁵⁴ Mr Highfield, Private capacity, *Committee Hansard*, Canberra, 14 June 2017, p. 6.

¹⁵⁵ Mr Highfield, *Committee Hansard*, Canberra, 14 June 2017, p. 6.

¹⁵⁶ Ms Rosenzweig, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 6.

¹⁵⁷ The Tax Institute, *Submission 16*, p. 3.

¹⁵⁸ IGT, *Submission 5*, p. 16.

¹⁵⁹ IGT, *Submission 5*, p. 16.

software, digitisation and the streaming of services, such as the STP and simplified BAS, could 'reduce the value of tax practitioners'.¹⁶⁰

3.150 In his submission, the Inspector-General of Taxation rejected this view, noting that the ATO had taken seriously concerns about the utility of services and quality of communication with tax agents, which his Office had identified in its 2015 review of the role of tax agents and acknowledged the ATO's assistance to them.¹⁶¹ The submission further asserted, that:

The ATO's ongoing service delivery should not detract or dissuade taxpayers from seeking independent tax and legal advice on their tax affairs. The ATO cannot and should not be the sole source of advice for taxpayers.¹⁶²

Tax agents into the future

3.151 In regards to the future role of tax agents, the Inspector-General's submission also cited a recent OECD study which foreshadowed a transformation to a more strategic role, in the context of financial planning and business advice. Further, improvements in data analytics, predictive modelling and advanced design support systems might be expected to provide a basis for agents to provide this more tailored advice.¹⁶³

3.152 CPA Australia considered this process to be already well advanced:

Most tax professionals provide whole-of-business services and are no longer focused entirely on tax return preparation. In fact, for tax professionals, tax return lodgement is now often regarded as a by-product or the end result of better business advice and better automated processes and systems.¹⁶⁴

3.153 The Inspector-General identified the quality and reliability of ATO systems as an underpinning consideration in this transition.¹⁶⁵ The Inspector's submission also recommended that a more thorough review of this by an

¹⁶⁰ Taxation Practitioners Board, *Submission 9*, p. 2.

¹⁶¹ IGT, *The Australian Taxation Office's Services and Support For Tax Practitioners*, 2015, p. 2; see also ANAO, *The Australian Taxation Office's Management of its Relationship with Tax Practitioners*, 2002, p. 12, cited in IGT, *Submission 5*, p. 17.

¹⁶² IGT, *Submission 5*, p. 19.

¹⁶³ OECD, *Rethinking Tax Services: the Changing Role of Taxation Services Providers in SME Tax Compliance 2016*, p. 58, cited in IGT, *Submission 5*, pp. 19, 20.

¹⁶⁴ CPA Australia, *Submission 4*, p. 2.

¹⁶⁵ IGT, *Submission 5*, p. 20.

independent body, such as the Productivity Commission, could consider the broader cost implications for taxpayers of compliance, including further risk management and enforcement activities by the ATO.¹⁶⁶

3.154 At a hearing in Canberra, Tax Institute President Mr Matthew Pawson noted:

Intuitively, the no-return proposition infers there will be less work about for tax agents, and one would argue that this position is not in the best interests of our members. Possibly so. However, The Tax Institute is awake to the reality that the impact of disruptive technology is inevitably going to change the nature and role of the traditional tax adviser.¹⁶⁷

3.155 The Inspector-General of Taxation is currently undertaking a review of the role and future of tax practitioners which is due for release by June 2018. The Committee awaits the conclusions of that review for more industry specific views and directions which may impact taxpayer engagement with the tax system and engagement with tax practitioners specifically.

Tax agent portal and products

3.156 The ATO has made commitments to ensure that services available to tax agents support their real business practice needs into the future. Over the last decade, this has meant delivery of combined services in the Tax Agents Portal, ATO online and practice management software.¹⁶⁸ More recently, as discussed below, the focus has been on the necessary integration of the ATO managed portal with commercial practice products.

3.157 Tax intermediaries have had access to a dedicated tax portal since 2012, with refinements evaluated in the Committee's annual report review inquiries since 2014. In 2016, a schedule for trial and feedback on the phasing in of the new Practitioner Lodgement Service (PLS), and phase out of the old electronic system though to Tax Time 2017 was provided to the Committee.¹⁶⁹

¹⁶⁶ IGT, *Submission 5*, p. 21.

¹⁶⁷ Mr Pawson, The Tax Institute, *Committee Hansard*, Canberra, 6 September 2017, p. 2.

¹⁶⁸ ATO, *Submission 15*, p. 14.

¹⁶⁹ ATO, *Submission 1*, p. 20, cited in House of Representatives, Standing Committee on Tax and Revenue, *2016 Annual Report of the ATO, Performance Review 2015–16*, March 2017, p. 16.

3.158 During the current inquiry, Commissioner Jordan described recent progress (at late March 2017) noting the importance of the ATO's partnership in design with software developers:

The practitioner lodgement service...is to enable [agents] to do one lot of input from their client into their system which goes directly into our system. Instead of the two screens—I have my practice system and then I get onto the tax office—it is all one. So that should save a lot of back-office time. It might be more difficult for agents to charge for, because it is re-keying and it is not face-to-face time; it is just connectivity with us...

That is why we see that as a pretty important development to have fully up and running, but it does depend on the software providers working with us. We are happy to do a lot of the grunt work and develop a lot of the relevant coding and APIs, and provide them at no charge so they can then take it into their product.¹⁷⁰

3.159 Mr Olesen discussed the integration of commercial product interfaces with the tax agents' portal:

We have made the services available, but they are being integrated into the commercial software providers' software because it is their software that most tax agents use in their practice to run the practice. The goal...a tax agent would be able to run their entire practice off the practice management software that is provided by their commercial provider, and all the services that they need to access from us would be accessible through the practice management software that their software provider has provided them.¹⁷¹

3.160 The ATO's Chief Information Officer Mr Katf elaborated:

What we are providing is a platform that people can connect to. How they choose to do that, through what type of software, we have left open to them. At the moment, most of those are targeted to either tax agents or small business. There are some that are targeted at individuals and, therefore, they interact that way.¹⁷²

3.161 Deputy Commissioner Rosenzweig cited, as an example, a cash flow management product for small business and their agents:

¹⁷⁰ Mr Jordan AO, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 5.

¹⁷¹ Mr Olesen, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 5.

¹⁷² Mr Ramez Katf, Chief Information Officer, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 5.

One of the products that we have just been developing and piloting is a cash flow management product. That was really developed in response to the fact that small businesses do often struggle with cash flow and that then manifests in a lot of the problems that we see in the tax office...It is a tool that small business advisers as well as accountants can work through with their clients in a very practical way to help them manage their cash flow and get it back on track. — It is a product that we are going to white-label so that professional bodies and accountants can use it in their own way, as they think is most appropriate, with their clients.¹⁷³

- 3.162 The Inspector-General referred to recommendations made in his 2015 tax agent services review, that the ATO increase its use of modern modes of communication for tax practitioners, such as by introduction of unique identifiers or voice recognition, and by developing a ‘web chat functionality’ to provide tax practitioners with useful information.¹⁷⁴ The submission noted progress, with voice recognition now in place for taxpayers and the implementation of the Alex ‘virtual assistant’ who ‘understands conversational language and can clarify what you want and answer your questions.’¹⁷⁵
- 3.163 Feedback from agents and individuals on the Alex online tool, however, was mixed. Mr George Abernathy was frustrated by the tool’s limited comprehension of enquires and called for intelligent staff to be deployed.¹⁷⁶ CAANZ observed that: ‘Alex does not yet reflect artificial intelligence characteristics but is nonetheless based on software that learns from previous interactions with users. It will be interesting to see how the functionality of this virtual assistant will improve over coming years’.¹⁷⁷
- 3.164 CAANZ also critiqued the current utility of other online tools, noting:

In terms of accessing tax information and online assistance products such as tax calculators, a number of attempts have been made to improve the ATO website although the generally held view amongst our members is that the website remains very difficult for experienced tax professionals (let alone ordinary taxpayers) to find the information they need. Searches on the ATO

¹⁷³Ms Rosenzweig, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 6.

¹⁷⁴ IGT, *Submission 5*, pp. 31–32.

¹⁷⁵ IGT, *Submission 5*, p. 32.

¹⁷⁶ Mr George Abernathy, *Submission 24*, pp. 7, 10.

¹⁷⁷ CAANZ, *Submission 3*, p. 5.

website will often result in a confusing number of “hits”, many of which can be irrelevant.¹⁷⁸

Committee conclusion

- 3.165 Taxpayer engagement in Australia, on the basis of willing participation—reporting, lodgement and timely debt payment—is high. The proportion of taxpayers deliberately disengaging and those oblivious to the system appears to be small but there are hidden costs and losses, such as through refund churn, including of the GST, compliance costs in hiring tax professionals to provide clarity in a system dogged by complexity, or merely in duplicated compliance efforts.
- 3.166 The Committee notes the benefits which accrue to the tax administrator in richer and faster data transfer and in timely reporting and payments with the mandated use of payroll and super systems developed using standard platforms and ATO developed APIs. The Committee is aware of the initial cost burdens of complying with such policy decisions but also of the considerable benefits which accrue when tax compliance is embedded in activities naturally occurring in the course of business.
- 3.167 The Committee was nevertheless concerned that the ATO is seeking to provide services to end users to the exclusion of other providers. The view of the Committee was that the ATO should pursue a strategy of creating a platform that facilitates other providers to create services. Such an approach is not uncommon in information technology companies, the most commonly cited example being the Apple eco-system embodied in iTunes.
- 3.168 Evidence suggested that the ATO’s collaboration with software providers to enable free-design of tailored products for varied small business situations—providing the required data and information parameters are embedded in those systems—appears to be a model which is working for the co-developers.¹⁷⁹ It is unknown how satisfied businesses are with these solutions, given lack of direct evidence. However, the Committee heard there is considerable competition in the Australian market (around 70 software developers competing in general business suite products) which would encourage the development of desirable products—products that are easy to use, reduce duplication and ultimately reduce costs. This can only

¹⁷⁸ CAANZ, *Submission 3*, p. 5.

¹⁷⁹ The tax administrator and the software developers.

buttress willing participation in the small business sector. Measures to improve capacity to run seamless compliant operations in an increasingly non-cash environment will naturally foster tax and superannuation engagement.

- 3.169 The Committee anticipates the increasing demand for payment in electronic media is likely to reduce the opportunity for some currently cash dominant industries to disengage. Chapter 5 explores the cash economy and the prevalence of this in the small business sector.
- 3.170 With new digital platforms, more thorough pre-filing and access to a deductions management tool the majority of individual taxpayers now have the ability to relatively quickly and inexpensively prepare and lodge their tax returns digitally. Despite this, the Committee heard that nearly three quarters of individual taxpayers still engage a tax professional. Part of this may be due to impediments to digitally self-manage tax affairs like the 'ready access to adequate hardware, software and robust internet connections' while others may involve cyber-concerns. The Committee recognises other reasons for taxpayers not lodging digitally and this will be discussed further in Chapter 4. The Committee supports choice of constructive compliant engagement.
- 3.171 In addition, there are individuals who have complicated tax affairs where it may be unwise or most difficult to self-manage and these individuals would be expected to employ the services of tax professionals. The value of tax and accounting specialists in small business is reflected in the 95 per cent usage. A further discussion of the role of tax professionals and current threats to taxpayer engagement are explored in Chapter 6.

Tax regime simplification

- 3.172 As has been repeated throughout inquiry evidence, Australia's tax system is complicated—also detailed in previous tax system reviews—and would benefit from wholesale reform. The system has layers of incremental change and as such, any single change has collateral impacts.
- 3.173 However, the Committee accepts that the long-term maintenance of willing participation, that of engagement in the tax system, is significantly hampered by the underlying design of a complicated tax regime.
- 3.174 The Committee recognises the considerable in-roads made in the client engagement experience as suggested in recommendations detailed in section G4: 'Client Experience of the Tax and Transfer System' from the report of the

Australia's Future Tax System Review, May 2010. It is pleasing to see that citizen-centric tax engagement systems have been developed for individuals and small business with a focus on simplifying and tailoring information and reducing time and cost burdens.

- 3.175 With the integration of data from interdependent transfer system agencies as well as extensive third party pre-filing and tools to assist self-management of deductions, many individuals have the capacity to digitally self-manage their tax affairs. The system is also transparent in that the taxpayer knows the data that the ATO uses to pre-fill, and communication can be timely.
- 3.176 Likewise, small businesses have become the beneficiaries of business software packages with up-to-date and user-friendly interfaces developed by the professional software industry using ATO programming interfaces. This way, systems meet tax *and* business functionality and reduce costly duplication.
- 3.177 However, the Committee can see that positive taxpayer experiences are created by a positive tax regime framework, and that is a framework which balances simplicity with fairness.
- 3.178 As new technologies disrupt and transform commercial environments, new imperatives have arisen which will be addressed in Chapter 6, covering challenges and solutions. The Committee therefore believes it is timely for the Government to revisit consideration of Australia's broader tax regime and what reforms are required to place the Australian tax system in the best possible position, not only for domestic taxpayers but for all Australian residents.

Recommendation 1

- 3.179 The Committee recommends that a review of Australia's tax system should be undertaken before 2022, with the purpose of making recommendations on how to simplify the present tax system, in order to reduce both the quantum of tax law and improve comprehension and compliance by people without expertise in taxation law.**
- 3.180 This review is timely in light of the rapidly evolving digital environment, new commercial and financial platforms, increasing data volumes, identity and authentication threats and significant demographic and labour market challenges. All of these impact tax revenue and compliance.

- 3.181 Any future blueprint of Australia's tax system should follow the principles of simplification, transparency, sustainability and minimising of compliance burdens.
- 3.182 Given the challenges to tax law reform, in the immediate term, the Committee commends the ATO for its investment in sophisticated Application Programming Interfaces (APIs) for the refinement and improvement of online tools, such as the workplace deductions and contactor assessment tools, to increase the reliability of its assessment results and reduce risk to taxpayers.

4. Communication and compliance

Introduction

- 4.1 The *Reinventing the ATO—Program Blueprint* (March 2015) sets out five principles to transform the taxpayer engagement experience with the ATO:
- *Principle 1—Easy to get things right*
 - Contemporary digital experiences provided in the way people expect.
 - *Principle 2—Tailored experience*
 - Interactions are tailored and reflect people’s behaviour and circumstances.
 - *Principle 3—Excellent service*
 - Interactions are professional, respectful and timely.
 - *Principle 4—Fair and respectful treatment*
 - Contributing to effective tax and super systems is valued.
 - *Principle 5—Service delivered in the most effective and efficient way*
 - The ATO may not always be the provider of services to the community. The ATO will partner with service providers to deliver efficient and effective services.¹

¹ Extract, Guiding Principles of the Program, Australian Taxation Office (ATO), *Reinventing the ATO—Program Blueprint*, version 7, March 2015, p. 10
<www.ato.gov.au/uploadedFiles/Content/CR/downloads/program-blueprint-march-2015.pdf>
viewed 17 April 2018.

- 4.2 The document goes on to articulate key elements in building community confidence, ‘Through insight and tailored engagement’. In summary:
- The ATO has an early engagement approach to ensure people get things right initially, with mistakes less likely by pre-filling and integrating validation rules into software systems. These identify and prompt clients to review and correct mistakes themselves before they lodge.
 - Engagement matches client behaviour, for example if a genuine mistake is made the client and the ATO work together to resolve it, but if individuals, business, or intermediaries, decide to deliberately avoid or evade tax obligations they will be dealt with.
 - Tailored engagement based on risk, complexity and transparency level. These factors will determine the level of engagement from the ATO, low touch, medium touch or high touch.²
- 4.3 The previous chapter has discussed the ATO’s development and delivery of its digital lodgement segments and products, and their tailoring to specific client needs to streamline taxpayer engagement and make compliance easier. This chapter considers innovation in the ATO’s communication systems and methodologies under its Reinvention program, in particular its recourse to the theoretical and methodological tools suggested by the new science of behavioural economics.³ From this perspective the regulator’s primary focus is to use systems and services to promote taxpayers to voluntarily comply.
- 4.4 Given that a high proportion of taxpayers with straightforward tax affairs engage with the tax system through tax agents, this chapter considers whether policy change is required to address the high use of tax agents.⁴ The chapter also considers the compliance burdens for individuals engaging with the tax system and whether there are options for reducing this burden.

² For detail, see ATO, *Reinventing the ATO—Program Blueprint*, version 7, March 2015, pp. 12–13.

³ Identified as program 344 in Appendix 2, Table A.2 in Australian National Audit Office (ANAO) Report No. 15, 2017–18, *Costs and Benefits of the Reinventing the ATO Program*, November 2017. It was anticipated to cost \$1.5 million, actual cost identified by ANAO of \$805 000 between 2013–2014 to 2018–2019 years.

⁴ Mr Richard Highfield, *Submission 6*, p. 6. The submission notes that usage is one of the highest in the OECD. Note also in Chapter 2, pp. 31–33, the Commissioner of Taxation reflects the same view.

The role of behavioural economics insights

- 4.5 The ATO has, and is, increasingly informing its engagement with taxpayers through use of behavioural economic insights (BEI) techniques. The Behavioural Economics Team of the Australian Government (BETA), the Government's dedicated central unit within the Department of Prime Minister and Cabinet (PM&C), explained that:

...behavioural economics examines why people's actions deviate from the predictions of standard economic theory, which assumes that individuals always make choices that are rational and maximise their welfare. It combines experimental and field evidence with insights from disciplines such as psychology to develop richer economic models of decision-making.⁵

- 4.6 The OECD Tax Forum has advised that the capacity to bring together information from a range of sources to form a 'single view of the taxpayer' is supporting tax administrators to examine the 'type and timing of interventions that help taxpayers meet their tax obligations, including paying tax debts'.⁶
- 4.7 The new ethos of tax administrators in comparable nations is to design systems and communicate messages that prompt taxpayers to honour their obligations and provide accurate information, as the ATO puts it:

We are committed to putting taxpayers at the centre of everything we do by making it as easy as possible for them to get things right and difficult not to.⁷

- 4.8 According to behavioural economics experts, their approach enables tax administrators to better predict and influence the behaviour of particular taxpayers or taxpayer groups. For example, research has shown that increasing taxpayer confidence in the probity and fairness of tax systems increases the likelihood that people will honour their own tax obligations and willingly comply. Enforcement action against wrong doers and public disclosure of their activities supports the view that the compliance burden is

⁵ Department of the Prime Minister and Cabinet, Behavioural Economics Team of the Australian Government (BETA) Section, *Submission 18*, p. 1.

⁶ OECD, *Tax Administration 2017 Comparative Information on OECD and Other Advanced and Emerging Economies*, September 2017, p. 30 <www.oecd.org/ctp/administration/tax-administration-23077727.html> viewed 11 January 2018.

⁷ ATO, *Commissioner of Taxation's Annual Report 2016–17* [here after ATO Annual Report 2016–17], p. 12.

being fairly shared. In addition to motivating taxpayers to meet their own obligations, it can reduce tacit acceptance of tax avoidance in the community, such as though acceptance of illegal cash paid activity or under disclosure.

Behavioural economics methodology

4.9 The Behavioural Economics Team of the Australian Government (BETA) has been charged with building capacity across the Australian Public Service to apply behavioural economics approaches to policy, program and service development with a view to outcome improvements. BETA has been in operation for two years as at February 2018.

4.10 The results of behavioural economics insights are difficult to attribute directly to outcomes because people make decisions on the basis of many environmental and personal factors. BETA senior officers appeared at a hearing in Canberra and gave evidence about the role of the unit and how it tests for ‘cause-and-effect’ improved outcomes using randomised controlled trials.⁸

4.11 BETA’s submission advised that randomised controlled trials work by splitting testing into two population groups—a control group and an intervention group—and measuring the results for both. The submission explains:

A key pillar of behavioural economics is to test the application of potential biases and finding ways to mitigate or harness those biases that may prevent people from acting in their own best interest. Behavioural economics relies on rigorously testing the effectiveness of a policy intervention by using randomised controlled trials. Trialling takes account of the social context and any nuances in the policy area concerned. Increasingly, the policy development process requires that policies are underpinned by evidence, and randomised controlled trials are one avenue through which strong empirical evidence can be gathered.⁹

4.12 As this is a relatively new policy application in Australia and the results are achieved over longer time frames, the reports of the effectiveness of such methods are derived from overseas experience, principally from the United

⁸ Refer Department of the Prime Minister and Cabinet, BETA Section, *Submission 18*, p. 2 and <www.pmc.gov.au/domestic-policy/behavioural-economics> viewed 7 March 2018.

⁹ BETA, *Submission 18*, p. 2.

Kingdom where the first Government BEI unit, the UK Behavioural Insights Team (BIT), was established.¹⁰

- 4.13 However, Professor Hiscox, Head of BETA, observed that the ATO has been applying behavioural economics type principles to its taxpayer engagement approaches well before the discipline was formally recognised in policy development and citizen engagement. He said:

Before behavioural insights were embraced as a new, unique tool, Australia had implemented a range of policy and service delivery reforms that are compatible with behavioural insights theory. Default settings, such as pre-filled tax returns, are an extremely good example of this, saving taxpayers' time and making it easier and simpler to comply with the rules. The ATO has been one of the pioneers of the world in this area.¹¹

Effectiveness of ATO behavioural insights measures

- 4.14 The ATO advised that it has been applying behavioural insights for a number of years to achieve a range of outcomes, including to:
- encourage taxpayers to lodge and report, plus pay debts;
 - encourage taxpayers to shift to digital interactions;
 - encourage taxpayers to adopt new policies/obligations;
 - encourage willing participation and deter non-compliance by taxpayers; and
 - improve staff engagement and internal operations.¹²
- 4.15 BETA has highlighted the ATO's pre-filling of data for tax lodgements as consistent with the behavioural insight that individuals are more likely to comply when compliance is made as easy as possible. This also enhances the likelihood of accuracy of self-assessment.¹³
- 4.16 Another successful focus for the ATO has been the use of behavioural insights in communications to improve debt re-payments. The ATO

¹⁰ See Behavioural Economics, PM&C, <www.pmc.gov.au/domestic-policy/behavioural-economics> viewed 7 March 2018.

¹¹ Professor Hiscox, PM&C, *Committee Hansard*, Canberra, 10 May, 2018, p. 9.

¹² ATO, *Submission 15*, p. 15.

¹³ United States Inland Revenue Service (IRS), *Behavioural Insights Toolkit*, p. 25, and see BETA, *Submission 18*, pp. 3–4.

examined the language, structure and layout of a number of debt letters to increase payment compliance by being clearer about what taxpayers need to do and the consequences of not paying.¹⁴

4.17 The Inspector-General of Taxation has noted that the ATO is also using behavioural insights in developing a 'Debt Engagement Framework' which supports re-engagement with taxpayers in telephone contact by helping them understand and manage their payment obligations.¹⁵

4.18 The ATO advised that personalised text messaging had been a recent focus of this debt recovery work. Under the 'Purposeful First Action' model, where taxpayers receive more flexible or firmer responses based on analytics of their previous behaviours:

For example, we use various behavioural insight approaches to help people repay debts. In 2015-16, we issued 540 000 text message reminders to clients to pay on time. The use of reminders increased payments on time and led to payment plans being set up earlier than usual. Through this activity, \$949 million was raised, and this strategy of gentle reminders to habitual late payers is now part of our business-as-usual approach.¹⁶

4.19 The ATO has also used preventative text (sms) payment reminders to taxpayer businesses likely to 'pay late or not at all'. These reminders have also been sent to those who have not paid after a lodgement due date has passed.¹⁷

4.20 In addition, the ATO, within myTax, is focussing on 'real time analytics' to provide information to taxpayers on whether their workplace deduction amounts appear high relative to their peers. These taxpayers, using the myDeductions¹⁸ app, receive messages within the application to prompt appropriate action when it appears data input may not be authentic. For example:

In 2016 we began to use pre-emptive prompts that leverage the concept of transparency. For example, pop-up messages in myTax let taxpayers know if their work-related expense claims appear out-of-step with their peers,

¹⁴ Inspector-General of Taxation (IGT), *Submission 5*, p. 34.

¹⁵ IGT, *Submission 5*, p. 35.

¹⁶ ATO, *Submission 15*, p. 15.

¹⁷ ATO, *Submission 2*, Inquiry into 2016-17 ATO Annual Report, p. 16. In 2016-17 560 000 reminder sms texts were sent which resulted in \$800 million in payments.

¹⁸ As outlined in Chapter 3.

enabling them to review their deductions before lodgement of their tax return.¹⁹

- 4.21 A new behavioural insights mechanism in this area will soon empower the ATO to disclose to credit reporting bureaus the tax debt information of businesses who have not ‘effectively engaged’ with the tax administrator to resolve debt issues. This will provide a powerful incentive for businesses to work on their debt arrangements and with the ATO on payment plans or jeopardise their business name and trading and credit terms which have in the past been unmarred by a tax debt.²⁰
- 4.22 Mr Paul Drum, Head of Policy, CPA Australia, provided an example of how different levers in a tax system, in this instance a GST or VAT, can work to motivate compliance outside of more direct enforcement methods
- If you look at the Australian experience...there were hundreds of thousands more registrations for the GST than they [the ATO] knew there were businesses in Australia. — Some of that was because—and this is behavioural economics at work—people are quite happy not to pay their income tax, but they are sure as hell going to claim back their input tax credit. So they wanted their 10 per cent back on their business input. — It drew a certain number of business into the net and the tax office at the time reported that there were businesses that came out and said: “We want to come clean”.²¹
- 4.23 The Committee also considered evidence presented that urged some caution in the application of behavioural insights, in particular nudge policies, for two main reasons.
- 4.24 Firstly, the use of real time analytics may lead people to repeatedly test or game the system, for example in the myDeductions app, such that they reduce the value of their claim until the point that the system no longer generates a warning.²²
- 4.25 Mr Michael Croker of Chartered Accountants Australia and New Zealand (CAANZ) warned against this:

¹⁹ ATO, *Submission 15*, p. 15.

²⁰ ATO, *Submission 2*, Inquiry into 2016-17 ATO Annual Report, p. 17. The ATO will consult with the Inspector-General of Taxation before a business’s tax debt is disclosed.

²¹ Mr Paul Drum, Head of Policy, CPA Australia, *Committee Hansard*, Melbourne, 17 July 2017, p. 11.

²² Mr Michael Croker, Tax Leader Australia, Chartered Accountants Australia and New Zealand (CAANZ), *Committee Hansard*, Melbourne, 17 July 2017, p. 7.

There is the sense, the idea, that you do it yourself online, with MyTax for example—you type in work boots at \$1,000 and a nudge message comes up and says, ‘No, that’s just beyond the pale’, so then you type in \$800 and then \$600—and that you experiment with online claiming and try to check out when do you come into the benchmark that’s acceptable.²³

4.26 Secondly, there is the chance that disengaged individuals who have no, or limited understanding of the tax system are ‘nudged’ into it inappropriately or with little support, and thus may make poor tax driven decisions. This is something increasingly likely given the Australian tax system’s interactions with social welfare and data matching.²⁴

4.27 The submission from Dr Chardon, Dr Freudenberg and Professor Brimble, taxation and finance law academics from two Queensland universities, suggested:

The ‘nudge’ concept comes with the risk that taxpayers may have no cause to engage with the tax system over many years and then suddenly be forced to engage with a system with which they have had little interaction with over their adult life. We therefore submit that any automated or ‘nudge’ systems be balanced with greater taxpayer education about the basic concepts of tax and superannuation that need to be understood in order to prevent poor financial decisions and to ‘make decisions in their best interests’.²⁵

4.28 This concern over the financial literacy of the taxpayer and the understanding of their circumstances being a consideration in impersonal dealing with the ATO was echoed by ETax Accountants, who argued:

...it should not be a role undertaken by the ATO, nor any 3rd party not directly involved with the individual taxpayer, to tell a taxpayer how their affairs might fit into a certain “box” —especially when those parties might make such recommendations with no knowledge of any but the roughest details of the individual’s tax and financial affairs, or without qualifications to offer such guidance (as might arguably be the case with, for example, some advice dispensed to taxpayers by ATO call centre staff or 3rd party employees at ATO contracted call centres).²⁶

²³ Mr Croker, CAANZ, *Committee Hansard*, Melbourne, 17 July 2017, p. 7.

²⁴ For example, making decisions which have significant tax implications (retirement planning and investments) or actions to meet eligibility requirements for welfare.

²⁵ Drs Toni Chardon, Mark Brimble, and Brett Freudenberg, *Submission 20*, p. 2.

²⁶ ETax Accountants, *Submission 7*, p. 2.

4.29 Given potential concerns that some behavioural economics mechanisms may not act in the best interests of the taxpayer, the Inspector-General of Taxation recommended that the ATO could review current behavioural insights work by BETA, the NSW Government's Behavioural Insights Unit (BIU) and in other comparable service delivery agencies:

...in particular any work being done outside of the debt area, how it is assisting taxpayers to make decisions in their best interest. In doing so, [it] could consider the taxpayer's best interest, how it varies across different taxpayer groups and how it is determined. In this regard, [it] may find learnings from the UK in relation to practising mindfulness by public policy makers particularly useful.²⁷

Committee comment

4.30 The Committee has considered the concerns voiced in relying too heavily on behavioural insights research in taxation engagement, along with the fact that many of the policies attributed to behavioural insights could be categorised as sound tax administration approaches that reflect current technology, rather than carefully created policies based on behavioural economics.

4.31 The evidence appears to be that behavioural insights and the ATO's partnership with BETA could provide a useful adjunct to conventional approaches in some policy areas, and the Committee is supportive of these policy approaches, however there was evidence presented that urged some caution in their application. An example of an unintended response to inbuilt system nudges is the incidence of 'gaming' deduction applications to determine the highest allowable deduction.

4.32 Notwithstanding this possibility, the Committee was impressed with the benefits that behavioural economics brings to policy development and implementation. The Committee was particularly encouraged by the outcomes of policy implementation being tested using control randomised trials. The Committee would encourage the ATO to examine how it could use such techniques and test them against current implementation programs to understand if it materially changes implementation strategies.

4.33 The Committee otherwise considers that the current level of investment in behavioural insights approaches by the ATO appears to be reasonable given

²⁷ IGT, *Submission 5*, p. 36.

the relative infancy of the discipline and the lack of international evidence to support its medium to longer-term effectiveness.

- 4.34 Behavioural insights policy appears to be a strategy appropriate for people on the margin or tipping point of tax non-compliance, not entrenched tax evasion. Its benefit may be that it is a relatively small investment in nurturing a tax compliance culture and thus keeping the majority of taxpayers on the right path.

Recommendation 2

- 4.35 **The Committee recommends that the ATO should continue to deploy behavioural insights approaches to increase taxpayer engagement. The ATO should, however, examine and report on the results of these programs or activities, recognising their limitations within an overly complex tax system.**
- 4.36 Until more evidence of its long-term effectiveness is available, the Committee would not encourage the ATO to invest in radical changes in administration based on behavioural insights. There is, however, potential to build on behavioural insights trialling methodologies, and other proven performance focussed systems, to drive improvements in ATO performance and services.
- 4.37 The benefits of such trials are obvious in implementing new systems. As such the Committee encourages the ATO to use such systems for both future implementation and ongoing improvement projects.

Recommendation 3

- 4.38 **The Committee recommends that the ATO should make greater use of behavioural insights techniques, such as randomised controlled trials, before full implementation of new initiatives to determine if such changes are indeed better than current practices, and if so, which changes are the most effective.**

The ATO could also run continuous trials (using methodology such as, but not limited to, the Lean Six Sigma system²⁸) on communication

²⁸ Six Sigma is a disciplined, data-driven approach and methodology for eliminating defects (driving toward six standard deviations between the mean and the nearest specification limit) in any

platforms and channels to ensure that its systems are constantly being tested and improved.

Behavioural insights in other service agencies

4.39 Notwithstanding the recommended caution in this area, it is noted that the ATO works with BETA to promulgate of the behavioural insights principles which inform the ATO's program design, development and implementation to other services agencies. These BEI principles include:

- designing processes, systems and approaches that minimise effort to meet obligations;
- providing certainty about our procedures, timeframes and how to fulfil obligations;
- targeting our approach and personalising messages;
- providing transparency about what we know and what we are doing; and
- informing people of how their behaviour compares to the general population.²⁹

4.40 The ATO has stated that in establishing and refining its approach it has looked to the experiences of like-minded tax agencies including from Canada, Singapore, the USA, New Zealand and the United Kingdom.³⁰ It is also noted that the ATO participates in the OECD's Forum on Tax Administration, and has maintained that compared with other tax administrators, is in advance in achieving a comparatively favourable collectable debt to percentage of collections using its work on debt letters.³¹

4.41 Chapter 2 provides examples of advances to date overseas in comparable countries, notably a research partnership between Belgium and the London Universities to trial debt letters, similar to the ATO's work, as well as advances in Sweden and Estonia on pre-filing, and the use of telephone

process – from manufacturing to transactional and from product to service. See Six Sigma <www.isixsigma.com/new-to-six-sigma/getting-started/what-six-sigma> viewed 24 July 2018.

²⁹ ATO, *Submission 15*, p. 15.

³⁰ ATO, *Submission 15*, p. 15.

³¹ ATO, *Submission 2*, Inquiry into the 2016-17 Annual Report of the ATO, p. 16.

campaigns in Canada, the United Kingdom and Norway, and reminder calls in Belgium.³²

- 4.42 To assess the effectiveness of the ATO's promulgation of measures to other federal service agencies, the Committee sought evidence from a variety of such agencies but most declined to submit information on the basis of the infancy of their insights application work, or its application in areas they considered to be unrelated to the Committee's inquiry into federal tax administration.³³
- 4.43 In the absence of direct evidence received on the service delivery strategies of other agencies, the Committee referenced research work submitted to the Regulatory Institutions Network at the Australian National University. In particular, the Network's *2010 Occasional Paper No. 15* examined responsive regulation approaches in a variety of federal and state government agencies and overseas agencies, including the New Zealand Inland Revenue (NZIR).³⁴
- 4.44 The NZIR work considered the approaches of these administrators and regulators, who are mostly using a regulatory pyramid approach where the 'light touch' strategies like education, persuasion and advisory initiatives sit at the base of the pyramid, with heavier hand enforcement and punitive interventions progressing to the apex of the pyramid.³⁵
- 4.45 The occasional paper assessed the ATO's current regulatory approach under the 'Cooperative Compliance Model',³⁶ which is also a pyramid-based approach, and concluded that by comparison: '[the ATO's] Model

³² See for references OECD, *Tax Administration 2017 Comparative Information on OECD and Other Advanced and Emerging Economies*, 29 September 2017 (hereafter OECD, *Tax Administration 2017*), pp. 56, 159–60.

³³ Input from the New South Wales Government's Behavioural Insights Unit (BIU) and the revenue agency in Victoria was also sought as both administrations had utilised the work of the UK Behavioural Insights Team's Australian office.

³⁴ C Wood, M Ivec, J Job and V Braithwaite, 'Applications of Responsive Regulatory Theory in Australia and Overseas', Regulatory Institutions Network, Australian National University (ANU) *Occasional Paper 15, June 2010*, p. 13.

³⁵ According to the authors, administrators should focus most efforts at the base of the pyramid.

³⁶ For reference, the ATO Compliance Model is at <www.ato.gov.au/about-ato/about-us/in-detail/key-documents/compliance-model/> viewed 22 March 2018.

emphasises the need to better understand why people are not complying, and to develop appropriate and proportionate responses'.³⁷

4.46 The ATO has formulated a tool to analyse taxpayers' reasons for behaving in a particular way, which is based on Business, Industry, Sociological, Economic and Psychological reasoning (BISEP).³⁸ The BISEP model was first developed 20 years ago for the 1998 Cash Economy Task Force to better respond to the systemic causes of tax non-compliance. It conceptualises clients under four main categories:

- 1 disengaged clients who have decided not to comply;
- 2 resistant clients who don't want to comply;
- 3 captured clients who try to comply, but don't always succeed; and
- 4 accommodating clients who are willing to do the right thing.³⁹

4.47 The ATO also publishes a 'Statement of Intent' (which is a response to the Government's 'Statement of Expectations' of the administrator) which outlines its relationships with the Government, the Minister, the Treasury and other regulators and how it will be accountable and transparent and its governance and financial procedures.⁴⁰

4.48 The ATO's Compliance Model, as previously discussed, is based on a pyramid of engagement. The Reinventing the ATO Program Blueprint details the future direction of the agency and the expected change in client experience. However, it appears that the ATO does not currently have a contemporary document which outlines in practical terms how it will engage with taxpayers along the spectrum of compliance or uncertainty in interpreting the law it administers over time.

³⁷ C Wood, M Ivec, J Job and V Braithwaite, 'Applications of Responsive Regulatory Theory in Australia and Overseas', Regulatory Institutions Network, ANU *Occasional Paper 15, June 2010*, p. 13.

³⁸The model was first developed 20 years ago through the 1998 Cash Economy Task Force which undertook to understand and respond to systemic causes of tax non-compliance through the cash economy, see C Wood, M Ivec, J Job and V Braithwaite, ANU *Occasional Paper 15, June 2010*, p. 13. See also ATO Compliance Model, viewed 22 March 2018.

³⁹ C Wood, M Ivec, J Job and V Braithwaite, ANU *Occasional Paper 15, June 2010*, p. 13.

⁴⁰ The ATO's Statement of Intent <static.treasury.gov.au/uploads/sites/1/2017/06/ATO_Statement_of_Intent.pdf> viewed 22 March 2018.

- 4.49 A public engagement strategy used by another Federal government agency provides a possible approach. The Civil Aviation Safety Authority (CASA) publishes a 'Regulatory Philosophy' which outlines the principles by which it will administer its regulatory functions.⁴¹ This regulatory philosophy is referenced in the Minister's Statement of Expectations to CASA and it provides a useful benchmark against which external stakeholders can judge CASA's actions and provides CASA staff with clear and codified expectations in discharging its regulatory functions.
- 4.50 In considering whether publication of a regulatory philosophy would be appropriate for the ATO, the Committee notes recommendation 112 of the *Australia's Future Tax System* (AFTS) report which suggested that:
- The government should commit to a principles-based approach to tax design as a way of addressing the growing volume and complexity of tax legislation, and as a way of helping those laws to be interpreted consistently with their policy objectives.⁴²

Committee comment

- 4.51 The Committee considers that the most relevant insights would be derived from the experiences of tax agencies in comparable countries and that the ATO would be in a strong position if it was able to demonstrate that it had benchmarked its key publications and forms against measures in comparable countries using behavioural insights approaches.
- 4.52 The ATO and BETA through their partnership could:
- monitor taxpayer engagement strategies, based on behavioural economics, in relevant countries and consider for implementation in Australia those policies with proven effectiveness compatible with the Australian system;⁴³ and
 - review existing ATO engagement strategies against behavioural economics benchmarks, to test consistency with best practice, and assess

⁴¹ Refer CASA <www.casa.gov.au/about-us/standard-page/our-regulatory-philosophy> viewed 3 March 2018.

⁴² *Australia's Future Tax System (AFTS)– Report to the Treasurer, December 2009, Part One, Overview*, p. 102.

⁴³ For example, in the USA that letters which included an appointment with personal call-in time increased call-in rates by 23 per cent, US IRS, *Behavioral Insights Toolkit*, p. 17. <www.irs.gov/pub/irs-soi/17rpirsbehavioralinsights.pdf>

the implications of shortfalls for tax engagement—and ultimately compliance and revenue—from ineffective approaches.

- 4.53 In addition, the Committee sees value in implementing AFTS recommendation 112 and suggests that the ATO follow the example of other Federal administration service providers by preparing and publishing a ‘Regulatory Philosophy’. This would be consistent with the ATO’s current principles-based approach to tax administration, but set benchmarks for the ATO to better assess how it assists taxpayers make decisions in their best interest, and how best to motivate that engagement.

Recommendation 4

- 4.54 The ATO consider adopting a Regulatory Philosophy to codify the principles on which it will administer tax laws and engage with taxpayers.**

- 4.55 A regulatory philosophy could provide the approach to the administration of the current tax law rather than forming the basis of tax law changes. It would be a philosophy of client engagement now and into the future. The purpose of such a philosophy would be about taxpayer engagement with the tax system and tax administrator—and fair administration of tax law. However, it may also be a useful starting point from which the Government could build to form principles for the design of new tax laws.

Educating the community

- 4.56 The foundation of effective taxpayer engagement is having at least basic levels of taxation system literacy. This was highlighted in the submission from Queensland academics Dr Toni Chardon et al,⁴⁴ which argued that improving tax and financial literacy across the community is fundamental to increasing voluntary engagement. Further, this is not just at the school level but available at all life-stages.⁴⁵
- 4.57 As at June 2015 the proportion of Australia’s resident population born overseas was estimated to be 28.2 per cent and many from diverse non-English speaking backgrounds.⁴⁶ Of the 2015–16 intake of migrants, of

⁴⁴ Dr Toni Chardon et al, *Submission 20*, p. 1.

⁴⁵ Dr Toni Chardon et al, *Submission 20*, p. 1.

⁴⁶ Australian Parliamentary Library, *Migration to Australia: a Quick Guide to the Statistics*, updated 18 January 2017.

189 770, 68 per cent came as skilled migrants, and so would be deriving income and required to have an understanding of Australia's tax and superannuation systems.⁴⁷

- 4.58 The Commissioner of Taxation outlined the ATO's response to the diverse needs of taxpayers in the community in the foreword to its primary submission:

As part of our holistic approach to engagement, our digital push is complemented by a refreshed face-to-face strategy. We have opened up new avenues for our clients to engage and interact with us—showing a friendlier face of the ATO and providing help in the form of 'show me how' sessions for small businesses and agents in both regional and metropolitan locations. We also continue to conduct our schools and migrant education programs which help young people and new arrivals learn about and engage with the tax (and super) system by connecting teachers with resources and expert tax officers.⁴⁸

- 4.59 The Institute of Public Accountants (IPA) maintained that broad education needs to occur at the grass-roots level to support tax literacy and effect cultural change towards compliant behaviour. Some approaches it suggests include:

- mandating electronic transactions;
- whole of government education, not just by the ATO—tax is 'the price for a civilised society';
- educate children about this in school curriculum;
- imposing penalties on those without a valid Australian Business Number (ABN);
- warn of the dangers of cash transactions—poor workmanship, health and safety, legal implications;
- that retailers upload daily transactions to the ATO; and
- a domestic tax amnesty, offering reduced penalties.⁴⁹

- 4.60 Dr Chardon and et al cited research indicating that although Australians are broadly tax literate, they find basic tax concepts more difficult to understand than basic financial concepts. Specifically, tax areas which are poorly understood include the rate of the super-guarantee, the difference between deductions and offsets, and broad concepts of capital gains. It was also

⁴⁷ In addition, 17 555 arrivals were from the humanitarian stream, many of working age.

⁴⁸ 'Commissioner's Forward', ATO, *Submission 15*, p. 5.

⁴⁹ IPA, *Submission 2*, pp. 6–7.

found that groups with a greater engagement with the tax system, for example small business owners, had higher tax literacy.⁵⁰

- 4.61 These experts therefore argued that a developed education program is necessary to address deficient knowledge in this area:

We argue that opportunities to educate and inform taxpayers at various stages in their education and work life should be encouraged and should focus on those areas identified as being poorly understood by taxpayers in our research and those areas that can best help taxpayers 'make decisions in their best interests'.⁵¹

Committee comment

- 4.62 As discussed previously in this report, comparable tax jurisdictions, such as the UK and NZ, have recognised that educating the community is an important support to behavioural insights measures. This is both to promote positive attitudes to tax compliance and to inform people about the nature and values of the tax system, as well as their obligations.
- 4.63 The Committee is aware of concerns among taxpayers that some segments within our society are not paying their 'fair share'. If this concern became widespread, and firmly held, it could undermine the very nature of Australia's low touch compliance environment. As such the Committee views it as critically important that while the ATO explains what measures it is taking to ensure integrity, it also educates people that non-compliance is very low, and that fairness in the system is a priority focus.
- 4.64 Noting the research results presented by Dr Chardon et al, the Committee also sees potential for more work to be done to determine whether high profile allegations of non-compliance (the majority of which are in fact compliant, and the result of people's misunderstanding between concepts such as revenue and profit) are undermining people's confidence in the system.

Information and transparency

- 4.65 One of the key recommendations of the AFTS report (under Category 9, 'A More Open, Understandable and Responsive Tax System'), was that not

⁵⁰ Dr Toni Chardon et al, *Submission 20*, p. 1.

⁵¹ Dr Toni Chardon et al, *Submission 20*, p. 1.

only should the tax system be responsive to threats as they arise but that it should be understandable—‘with citizens having clear rights to information on the tax system and their experience with it’.⁵² Presumably this provides context, promotes taxpayer ‘buy-in’, and ultimately supports compliance.

- 4.66 The report also suggested that citizens should be able to access ‘through a suitable choice of channels, comprehensive and timely information on their tax and transfer affairs’⁵³ and how these outcomes may have arisen and be affected by the choices they make. The Committee notes the ATO has come a long way in providing this offering through digital channels like myTax.
- 4.67 Additionally, the AFTS report recommended that Governments should make data and analyses of taxes and transfer payments publicly available to ‘inform and encourage community debate about the performance of the tax and transfer system’. The ATO does make available sample taxpayer datasets for research purposes and discloses its current research projects on the agency’s website, however this detail is not available online. Citizens are asked to email the ATO Corporate Research Area for this information.⁵⁴
- 4.68 The Committee sees benefit in the ATO adopting a more transparent approach to its research and findings, and should publish online information on status updates and data relating to its research.

Face-to-face with small business

- 4.69 The Commissioner of Taxation has noted his support for continued face-to-face liaison with the small business community to assist them with business engagement issues and tax literacy, and to provide feedback about the tax system. He stated:

We also have in place a range of channels and forums for taxpayers to voice their feedback and views about the tax system. For example, our Small Business Consultation Panel has more than 500 small businesses who are willing to use their practical insights to help us design an improved experience for others in their market segment. We also have our ‘Let’s talk’ platform where any member of the community can contribute ideas and have their say on tax and superannuation topics, and we have an online testing environment

⁵² *AFTS—Report to the Treasurer*, December 2009, Part One, Overview, p. xxiv.

⁵³ *AFTS—Report to the Treasurer*, December 2009, Part One, Overview, p. xxiv.

⁵⁴ See ATO, Current Research Projects <www.ato.gov.au/about-ato/research-and-statistics/current-research-projects/> viewed 28 February 2018.

called 'ATO Beta' that lets users test and provide feedback on our new digital offerings.⁵⁵

- 4.70 In its previous annual report review the Committee recommended the ATO ensure the continuation of small business 'fix it squads' to support these businesses through digital transition.⁵⁶ The ATO's submission to the current review, reported:

We continue to lead the cross-government small business 'Fix-it squads' comprised of taxpayers, intermediaries and government (federal and state) representatives who collaborate to design and implement a better experience. These Fix-it squads look at 'life events' take a whole-of-client approach and consider engagement for a variety of systems, regulations and government portfolios.⁵⁷

- 4.71 ATO Deputy Commissioner Digital Delivery Mr John Dardo acknowledged that there are key small business obstacles to streamlining compliancy obligations for the sector, but considered these could be partially overcome with more 'user friendly' systems. He said:

For some businesses, there is more work that needs to be done to help them understand that spending three hours trying to format a spreadsheet or trying to keep a paper record and doing everything three times might not be as easy as actually moving to something that is a bit more digital. That is one. The second one is they might genuinely be not digitally literate. That is increasingly shifting. In the past, if you looked at a Xero, MYOB or another screen, for example, you had to be a bit of a bookkeeper or an accountant type to try to navigate your way through it. As they produce more user friendly interfaces and more stuff that you can use on your iPhone or your iPad, we are seeing more businesses going, 'Cool, I think I can do this.'⁵⁸

- 4.72 He added, however, that 'in some cases, businesses feel they have an interest in not using the software or the accounting systems'.⁵⁹
- 4.73 Mr Oleson, head of the client engagement group ATO, emphasised that rather than trying to catch people out the ATO's approach is now to 'engage

⁵⁵ 'Commissioner's Forward', ATO, *Submission 15*, p. 5.

⁵⁶ Recommendation 7, *Review of the ATO Annual Report 2016: Performance Review 2015–16*, pp. xix, 57.

⁵⁷ 'Commissioner's Forward', ATO, *Submission 15*, p. 5.

⁵⁸ Mr John Dardo, Deputy Commissioner, Digital Delivery and Chief Digital Officer, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 19.

⁵⁹ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 19.

early with them and try and give people the tools and ability to serve themselves well'. He went on to explain:

...we are trying to do things upstream in real time and get people on the right track, because all our experience tells us that getting people on the right track early and giving them the tools that make it easy for them to meet their obligations is a far more productive way, in the long run, to run an effective tax system.⁶⁰

4.74 Ms Rosenzweig, small business section ATO, also highlighted the investment in face-to-face activity with small business over the 2017 year, largely in forum situations including showcasing services and new tools. She also highlighted tax essentials seminars which were run in tandem with programs co-developed with the Department of Industry for new businesses:

For any business that registers for an ABN and gives us their email address, we have a program of emails that go out in the course of the year. Rather than swamp them with a big pile of booklets when they start, they get some just-in-time information throughout the year about their obligations, particularly in that first year, to try and help them get off on the right foot.

Through that, we are able to talk to a lot of them about what they struggle with, where they find things challenging, and make sure that they have as much information and support as they need.⁶¹

4.75 Mr David Weickhardt, General Manager of MYOB Australia, referred to the strain put on small business in adjusting to the scale of transition in today's digital environment, including as new digital platforms are rolled out through the tax administration. He stressed that this should not be underestimated and that education support for small business was vital. He gave statistics on the impact of one significant example, the roll out of the Single Touch Payroll system:

It does require quite a bit of adjustment for small businesses going through it. There are one-off costs for people. The education comes back to the single touch payroll. We are anticipating multimillion dollars' worth of calls into our call centre as the single touch payroll gets rolled out. So government support

⁶⁰ Mr Neil Oleson, Second Commissioner, Client Engagement, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 6.

⁶¹ Ms Emma Rosenzweig, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 6.

in terms of education also making that transition easy for businesses is I, think, really important.⁶²

The potential of social media, SMS, voice biometrics and online assistance

- 4.76 As discussed previously in this chapter, the ATO is supplementing traditional mailed correspondence and phone calling with text messages and app prompts. The ATO also utilises other contemporary direct and indirect communication methods. One of these is social media platforms. The OECD has said that social media technologies have the potential to ‘bridge access and take-up gaps still faced by many traditional online government services’.⁶³
- 4.77 The ATO currently uses social media to provide the latest information on tax and superannuation changes, products and services, promote new initiatives, and to send reminders. It has also been used as a mechanism to warn of ATO phishing and other fraudulent scams. These messages are using Facebook, Twitter, LinkedIn and YouTube—for example, in early 2017 the ATO ran an on-line campaign entitled ‘Be aware of what you share’ which received 8.6 million views of advertisements, with over 800 000 video views and 12 600 clicks on these advertisements.⁶⁴ Another example is the ATO’s use of social media messaging to promote online lodgement options during the 2016 tax time period.⁶⁵
- 4.78 The Inspector-General of Taxation has identified Information and Communications Technology (ICT) improvements that the ATO could implement to assist taxpayers, many of whom regularly visit the ATO website.⁶⁶ As noted in the previous chapter, his 2015 review of services and supports for tax practitioners, the Inspector-General recommended that the ATO increase its use of ‘modern modes of communication’. Other recommendations considered the publication of practical online user guides

⁶² Mr David Weickhardt, General Manager, MYOB Australia Pty Ltd, *Committee Hansard*, Canberra, 27 October 2017, p. 15.

⁶³ Social Media Use by Governments: A Policy Primer to Discuss Trends, Identify Policy Opportunities and Guide Decision Maker (2014) p.3, cited in IGT, *Submission 5*, p. 30.

⁶⁴ ATO, *Submission 15.2*, pp. 9–10.

⁶⁵ IGT, *Submission 5*, p. 30.

⁶⁶ In 2015-16 there were 78 178 745 visits to the ATO website logged. ATO, *Submission 15.2*, p. 3.

for certain ATO platforms and developing a 'web chat functionality' to provide tax practitioners with useful information. The Inspector also advocated for simplifying proof of identity for tax practitioners through the use of unique identifiers or voice recognition.⁶⁷ The ATO has now implemented these recommendations.

- 4.79 Voice biometric identification is now available to all taxpayers. The ATO website notes that this technology offers a secure, faster and easier way to access ATO online services and telephony, and without the need for a password. As at Tax Time 2017 clients have used their voice as identification in over 53 000 instances and used the ATO app with voiceprint over 91 000 times.⁶⁸
- 4.80 In February 2016, the ATO launched a 'virtual assistant' on its website called 'Alex' who 'understands conversational language and can clarify what you want and answer your questions.' According to the Commissioner's 2017 Annual Report Alex has resolved more than 81 per cent of client queries at first contact since the launch.⁶⁹ However, Mr Abernathy, an individual taxpayer, discussed in his submission some deficiencies in the current virtual assistant approach.⁷⁰
- 4.81 The Inspector-General has not yet had an opportunity to examine the effectiveness of these new technologies. The Inspector-General of Taxation, (IGT), in his submission to the inquiry, invited consideration by the Committee of the ATO's experiences with these new innovations, suggesting the Committee may wish to 'explore any additional measures to enhance its service delivery to the community'.⁷¹
- 4.82 The ATO has also improved access for individuals and sole traders to view their business activity statements online and as such have the power to know and ability to pay activity statement debts online.⁷² The ability to

⁶⁷ IGT, *The Australian Taxation Office's Services and Support for tax Practitioners*, July 2015, List of Recommendations.

⁶⁸ See ATO, Authentication using Voice Biometrics <[//lets-talk.ato.gov.au/dspcommunity/news_feed/authentication-using-voice-biometrics](https://lets-talk.ato.gov.au/dspcommunity/news_feed/authentication-using-voice-biometrics)> viewed 7 March 2018.

⁶⁹ ATO, *Commissioner of Taxation Annual Report 2016–17*, p. 17.

⁷⁰ Mr George Abernathy, *Submission 24*, p. 8.

⁷¹ IGT, *Submission 5*, pp. 31–32.

⁷² ATO, *Submission 2*, Inquiry into 2016–17 ATO Annual Report, p. 17.

set up payment plans via the ATO website is now also possible for debts up to \$100 000 for both activity statements and income tax.

Nobody left behind—the challenges of digital transition

4.83 The future of tax administration is clearly a digital future but the smooth transition to it will take considerable effort by individuals, business and government. The ATO is open about its desire to encourage people to engage with it in a digital context. The supplementary submission to the inquiry states:

It is our intention to transition as many taxpayers as possible to digital services consistent with the approach for all government services.⁷³

4.84 As Mr Weickhardt of MYOB pointed out in evidence, this transition is not cost-free for small business nor for individuals.⁷⁴ As previously mentioned, there are considerable new fraud and identity threats in engaging in a digital world where increasingly sophisticated scams are conducted as this becomes a lucrative criminal activity.

4.85 The ATO's supplementary submission addresses the many support services provided for those who are less or not digitally engaged. The ATO recognises that digital exclusion extends beyond inaccessibility to internet services, noting that:

...some members of the community may be unable to interact digitally as a result of low levels of digital literacy, language, geographical or cultural barriers. Others choose not to interact with us digitally.⁷⁵

4.86 The ATO commits to providing support services for taxpayers to engage in the tax system in some way, whether the taxpayer is in a 'vulnerable' group, as identified above, or whether they prefer not to engage in a digital environment.

4.87 The Inspector-General of Taxation has received concerns from tax practitioners and taxpayers directly about digital delivery of ATO services. An example cited in the Inspector's submission is that of a church's inability

⁷³ ATO, *Supplementary Submission 15.2*, p. 3.

⁷⁴ Mr Weickhardt, MYOB Australia Pty Ltd, *Committee Hansard*, Canberra, 27 October 2017, p. 15.

⁷⁵ ATO, *Supplementary Submission 15.2*, p. 4.

to engage with the SuperStream system electronically ‘due to the remoteness of their location and their limited access to online services’.⁷⁶

- 4.88 Support services highlighted by the ATO include face-to-face assistance to engage in a digital manner, information sessions for groups, an inter-active voice response self-help phone lodgement service⁷⁷ and the continuation of supports for people wishing to lodge their return in paper format—of which 420 866 lodgements comprised in 2016–17.
- 4.89 Support services for paper lodgement include what used to be referred to as ‘TaxPacks’, now somewhat patronisingly referred to as ‘Care packs’⁷⁸ being sent to those who are not ‘digitally included’. In 2017 there were only 231 people considered to be in this category in Australia, the remaining paper lodgers who obtained paper forms and self-prepared had mostly either downloaded forms or obtained them from phoning the ATO publication service (and this is where myGov Shopfronts will redirect such a request).⁷⁹ Full details of non-digital support services are in the ATO’s supplementary submission under ‘Specific details of services offered to individuals’.⁸⁰
- 4.90 While the ATO is proud of its digital one-stop-shop, through myGov online, stating that ‘it is now possible for individuals to access a range of tax and superannuation services in one place, including lodging their tax return and activity statements...via ATO Online services’⁸¹ the myGov Shopfront does not offer, as standard practice, the basic non-digital tax resources.
- 4.91 Despite the assumption that the majority of people demanding paper forms are mature age, with paper-based lodgement being from older age groups, the Committee heard the contrary from representatives of *YourLifeChoices*, an online retirement ‘magazine’ for digitally engaged readers 55 plus. A survey undertaken in mid-2017 of its subscribers revealed how digitally attuned their audience was. For example, 43 per cent were using the ATO online tax

⁷⁶ IGT, *Submission 6*, p. 20. It is also worth noting that in addition to cultural barriers to digital interaction, as noted by the ATO, some minority religions oppose the use of computer technology altogether.

⁷⁷ Which business taxpayers can also access for certain things like lodging nil activity or nil GST statements.

⁷⁸ Comprising paper return forms and instructions.

⁷⁹ ATO, *Supplementary submission 15.2*, pp. 5, 7.

⁸⁰ ATO, *Supplementary Submission 15.2*, pp. 4–6.

⁸¹ ATO, *Submission 15*, p. 8.

services, while 57 per cent were using tax agents.⁸² Of those who used the ATO online services, 87 per cent said they found it easy to use.⁸³

- 4.92 Additionally, the ATO offers services to account for visual, hearing or speech impairment and for those in low income brackets—30 400 individuals were assisted through Tax Help programs supported by trained volunteers.⁸⁴ The Inspector-General of Taxation noted the positive feedback he had received through his Office's complaints handling function about the way: 'ATO officers seek to assist taxpayers where they can by, for example, providing printed copies of sections of the website and other digital information'.⁸⁵

Committee comment

- 4.93 The Committee believes the ATO is providing robust self-help services for those who wish to engage online. Alternative mechanisms for engaging with the tax system are available for the smaller proportion of taxpayers who are unable or unwilling to use digital services. The Committee stresses, however, that the ATO should remain cognisant of the many impediments to digital engagement, including for those with low income or compromised circumstances, as well for those who have been the victims, or near victims, of cyber-crime.
- 4.94 It is the Committee's view that people seeking to engage with the tax system should be welcomed and assisted in the most direct and appropriate manner. Citizens who make their way to an Australian Government Shopfront seeking a paper tax return form and/or accompanying completion information should not be redirected to ring an ATO publications service line or go to any other location to obtain basic tax forms or returns completion information. Australian Government 'myGov' Shopfronts are designed to be the one-stop physical public face of the Australian Government transfer, tax and support system. Forms and associated information for completing a simple tax return should be available at Shopfronts, if only by way of assisted self-download on site or inclusion on a dynamic 'Care pack' mailing list. A recommendation is made regarding this

⁸² Ms Kaye Fallick, Publisher, *YourLifeChoices*, *Committee Hansard*, Melbourne, 18 July 2017, p. 28.

⁸³ *Exhibit 2: YourLifeChoices*, Tax Survey Analysis, 18 July 2017.

⁸⁴ ATO, *Supplementary Submission 15.2*, p. 7.

⁸⁵ IGT, *Submission 5*, p. 20.

is in Chapter 6, along with a more general recommendation about enabling engagement according to taxpayer preferences.

- 4.95 The Committee also considers the new name for what is the closest replacement of the former TaxPack is discourteous and does not align with the ethos of the ATO reinvention.⁸⁶

Reliance on tax agents

- 4.96 As discussed elsewhere in this report, the proportion of taxpayers using tax agents is high by international standards, with Australia having one of the highest levels of reliance on tax practitioners of any OECD country. The ATO data shows that the use of tax agents is high even amongst those with simple tax affairs.⁸⁷ The ATO submission notes that 68 per cent of individuals not in business use a tax professional—despite 59 per cent of tax agent prepared returns (from the ATO Sample File 2013–14) disclosing income only from employment, pensions and investments and, as such, are relatively straightforward returns.⁸⁸
- 4.97 The question arises as to the role tax agents will play in advising taxpayers on lodgement of simple tax affairs now that legislative changes supporting significantly increased sharing of information for pre-filing have commenced. The explanatory memorandum to the Tax and Superannuation Laws Amendment (2015 Measures No. 5) Bill 2015, Chapter 4, ‘Third Party Reporting’ details the high level of data now at the ATO’s disposal for compliance and to prefill returns. These changes to the *Tax Administration Act 1953* (TAA 1953) came into effect for some transactions from 1 July 2016 while all transactions specified were captured on or after 1 July 2017:⁸⁹
- Payments of government grants;
 - Consideration provided for services to government entities;
 - transfers of real property;
 - transfers of shares;
 - transfers of units in unit trusts; and

⁸⁶ ATO, *Submission 15*, p. 4.

⁸⁷ Mr Richard Highfield, *Submission 6*, p. 8. The ATO submission notes 68 per cent of individuals use a tax professional.

⁸⁸ Mr Richard Highfield, *Submission 6*, p. 8.

⁸⁹ Tax and Superannuation Laws Amendment (2015 Measures No. 5) Bill 2015, Explanatory Memorandum, Chapter 4, Third Party Reporting, p. 59.

- business transactions made through payment systems.

4.98 The explanatory memorandum notes that:

The ATO now receives sufficient information so that in the majority of cases it is possible to completely pre-fill a simple tax return in relation to:

- Wage and salary data from employers;
- Government welfare payments from Centrelink and other providers;
- Interest income from financial institutions;
- Dividend income from share registries; and
- Medicare levy surcharge and private health insurance policy details from private health insurers.⁹⁰

4.99 Given the extent of the data that the ATO now receives to pre-fill tax returns, many of the 70-plus per cent of individuals who employ tax professionals to prepare their return already have significantly pre-populated return information. The continuing high use of tax agents in uncomplicated tax affairs is an important consideration when considering how taxpayers engage with the tax system and the associated compliance costs. A key question is whether such a high use of tax agents is appropriate and whether there should be a policy response to lower use.

4.100 A number of inquiry participants linked the high use of tax agents with the complexity of the tax system. The AFTS review report stated that:

- For many people, the personal tax system is complex not only because of the rates scale and the lack of a coherent definition of taxable income, but also because they must deal with a large suite of complex deduction rules, numerous tax offsets and a variety of exempt forms of income.
- Seventy-two per cent of taxfilers now seek advice from a tax agent, even though 86 per cent either claim no deductions at all or only claim work-related expenses, gifts and the costs of managing tax affairs. Australia's use of tax agents is high by international standards; second only to Italy's ... By contrast, the Nordic countries, which have pre-filling arrangements for tax returns, have low levels of tax agent use.⁹¹

⁹⁰ Tax and Superannuation Laws Amendment (2015 Measures No. 5) Bill 2015, Explanatory Memorandum, Chapter 4, Third Party Reporting, p. 60.

⁹¹ AFTS—*Report to the Treasurer, December 2009, Part One, Overview*, p. 31. Note Australia commenced pre-filling of electronic returns in 2007 to assist individuals with self-assessment obligations.

4.101 Some inquiry participants also argued that the ATO is inappropriately trying to reduce the reliance on tax agents by investing heavily in tools and services and that:

The ATO should not behave as a taxpayer-funded competitor against free-market Australian businesses, including against tax agents.⁹²

The tax return process

4.102 Another approach that could be taken to address the engagement of taxpayers through tax agents is to remove the requirement for individuals with simple tax affairs to lodge tax returns. This is a mechanism seen in other countries, for example, in Sweden. This was considered by the AFTS review which found that:

- an automatic standard deduction should be introduced to simplify people's interactions with the tax system and facilitate much greater levels of pre-filling of tax returns... and...⁹³
- In the longer term, opportunities exist to use 21st century technologies to make the system fairer, easier to comply with and more robust. Policy design should support greater automated reconciliation of tax affairs to reduce or remove the requirement for the taxpayer to collect their own information over the course of the tax year.⁹⁴

4.103 One submission highlighted a feature of modern tax systems, being that their administration is 'built on the principle of "voluntary compliance" – taxpayers are expected to comply voluntarily with their tax obligations *'with only limited intervention by tax officials'*.⁹⁵ As such, making interactions more streamlined and simple, especially if a large number of taxpayers can simply approve a statement of facts, would reduce duplicated efforts, time, cost and risk for all parties.

⁹² Etax, *Submission 19*, p. 4.

⁹³ *Australia's Future Tax System—Report to the Treasurer, December 2009, Part One, Overview*, p. 6. It also noted that 'However, to ensure that individuals with more complex affairs or high expenses are not disadvantaged, taxpayers would still have the option of substantiating a claim for all eligible expenses'.

⁹⁴ *Australia's Future Tax System—Report to the Treasurer, December 2009, Part One, Overview*, p. 6.

⁹⁵ Emphasis in submission—highlighting the onus is on the taxpayer to be accurate. See Mr Richard Highfield, *Submission 6*, p. 3.

4.104 Mr Pawson, President of the Tax Institute supported this view, saying it was feasible and practical to not only remove the requirement to lodge but also the discrepancy of a tax bill or refund:

It ought to be entirely possible to have a tax system where the majority of PAYG wage and salary earners can set and forget their tax obligations through the withholding system. By bringing together much-talked-about concepts of standardised workplace deductions, data warehousing by the ATO, integration of the Medicare levy and other relevant issues, it ought to be possible for a large proportion of taxpayers to have neither a tax bill nor a tax refund at the end of the financial year because the right amount of tax has been paid evenly throughout the year. Those taxpayers ought to be able to opt-in to a set-and-forget type system that does not require the lodging of a tax return, unless circumstances permit.⁹⁶

4.105 ‘Refund churn’, that is, where the tax collected during the year exceeds the tax assessed at year end thus triggering a tax refund after assessment of the lodged return, is a compliance burden to the tax system. It is also now an area ripe for refund fraud and with the expectation of faster refund turnarounds and high service standards, this maximises the chance of refund fraud being missed.⁹⁷

4.106 Much of these challenges would be eliminated through a better reconciled PAYG system which could be facilitated with greater simplification.

4.107 One option to enable such a system would be to remove the requirement of individuals with simple tax affairs (i.e. those without deductions) from being required to submit a tax return. This policy option could reduce the compliance cost to individuals from managing tax affairs and increase government revenue in the context of minimising the deductions for managing tax affairs. It would also bring forward any tax payments due (say for a PAYG taxpayer with a modest amount of interest income) who, with lodgement through a tax agent would enjoy an extended lodgement time and payment period. The extended timeframe for lodgement is an incentive to employ a tax agent over and above gaining tax expertise and the tax deductibility of the fee for service.⁹⁸

⁹⁶ Mr Matthew Pawson, The Tax Institute, *Committee Hansard*, Canberra, 6 September 2017, p. 2.

⁹⁷ Mr Highfield, *Submission 6*, p. 12.

⁹⁸ As noted in Mr Highfield, *Submission 6*, p. 5 – delays in standard lodgement (31 October for most individuals) has implications for transfer payments reliant on taxpayer year end data.

4.108 This approach would be consistent with the ATO digital strategy which could expand ‘to a “push” tax return for certain taxpayers, eliminating their need for lodgement’.⁹⁹

Communication and the compliance burden

4.109 The compliance burden of tax laws has been a key issue considered by most inquiries into the tax system. In 2015 Treasury estimated the compliance burden associated with tax laws for 12 million individuals at \$7.3 billion, \$18.7 billion for small business and \$7.6 billion for medium businesses.¹⁰⁰ For individuals this equates to an average annual compliance cost of approximately \$608.

4.110 For individuals who engage a tax agent, there was a range of evidence presented to the inquiry as to cost of compliance via a tax agent. Using ATO data for individual returns, the average tax affairs deduction for individuals is approximately \$370 per person, however, one tax agent submitted the average cost per individual taxpayer client as \$108.¹⁰¹ Another inquiry participant postulated a reasonable compliance cost for individuals with simple tax affairs would be \$400.¹⁰²

4.111 The compliance burden for individuals with simple tax affairs is likely to be in the range of \$200 to \$400 annually. The compliance burden is likely to increase with complexity such as by including investment income, deductions, foreign income, rental properties. For these individuals the compliance burden is likely to be within the Treasury range of \$600 or above.

International benchmarking

4.112 The Committee has examined the tax return form and instructions for individuals of a select group of other comparable countries—New Zealand, Canada, United States and the United Kingdom, as an indication of tax complexity and related compliance burden in these countries.

4.113 The analysis indicates that the annual tax return form in hard copy form is similar in detail and length and number of questions and fields among these

⁹⁹ ATO, *Submission 15*, Appendix 2, p. 7.

¹⁰⁰ The Treasury, *Stocktake of Regulation Final Report*, March 2015, p. 20.

¹⁰¹ Etax, *Submission 19*, p. 5.

¹⁰² Mr Richard Highfield, *Submission 6*, p. 9.

countries. However, it was found that the instructions or guidance for completing the form varied in length and complexity (Table 4.1).

Table 4.1 Individual Tax Return Instructions: Word Count

Country	Word count
United Kingdom	8 276
New Zealand	17 876
Australia	33 150
Canada	59 127
United States	90 500

Source: Secretariat analysis of country tax return instructions¹⁰³

- 4.114 The word count for the instructions accompanying the tax return form would not be a perfect indicator as to actual time that individuals would need to spend completing the tax return form. The Committee has sought actual compliance times when these are published, which was only available for the United States. The US IRS has published that for individuals the time to comply with taxation is approximately 13 hours annually.¹⁰⁴
- 4.115 In considering the compliance burden it is important to also take into account the number of individuals who are required to complete an individual return. In the United Kingdom the proportion of individuals required to complete a tax return is significantly lower than in Australia with only approximately 11 million of the population of 65 million required to complete a tax return in the United Kingdom.

¹⁰³ For sources see US Internal Revenue Service Form 1040A Instructions 2017 <www.irs.gov/pub/irs-pdf/i1040a.pdf>; Canada Revenue Agency General Income Tax and Benefit Guide 2017 – All Provinces Except Non-Residents <www.canada.ca/en/revenue-agency/services/forms-publications/tax-packages-years/general-income-tax-benefit-package/5000-g.html>; Tax Return Notes (2016-17) HM Revenue & Customs <[://www.gov.uk/government/uploads/system/uploads/attachment_data/file/615549/SA150-2017.pdf](http://www.gov.uk/government/uploads/system/uploads/attachment_data/file/615549/SA150-2017.pdf)>; Individual income tax return guide 2017 New Zealand Inland Revenue <www.ird.govt.nz/resources/a/2/a2a9e402-5825-44ef-af14-9d9436526f42/ir3g-2017.pdf>; Individual tax return instructions 2017, ATO <www.ato.gov.au/Forms/Individual-tax-return-instructions-2017/> all viewed 10 March 2018.

¹⁰⁴ USA IRS, *1040 Instructions 2017*, p. 102.

Committee conclusion

- 4.116 In this chapter the Committee has made recommendations in support of the review and refinement of the ATO's use of behavioural economic insights techniques, and supported considerations for a regulatory philosophy. As noted earlier in the chapter, 'The purpose of such a philosophy would be about taxpayer engagement with the tax system and tax administrator—and fair administration of tax law', rather than as a basis for tax law reform. The underpinning logic is to communicate more clearly to the taxpayer the nature of his or her 'best interests' in compliance and for the ATO to better understand the needs of each taxpaying sector.
- 4.117 The chapter has also considered issues of fairness and access related to the ATO's current communication methods and mechanisms for taxpayers, including small business, for disadvantaged groups and older people, and those who cannot or do not choose to access information online.
- 4.118 The Committee has discussed the impacts of the compliance burden in the context of making tax simpler to understand and in making the process easier, two integrated elements of improving voluntary engagement.
- 4.119 In relation to tax administration, the Committee notes that greater use of pre-filling in other nations has supported a shift to away from lodgement-based tax systems, and perhaps a lower level of reliance on tax agents for advice for those with simple tax affairs.
- 4.120 However, in Australia improvements in pre-filling have to date coincided with an increase in the use of tax agents. Perhaps there are other factors at play which the choice of lodgement by a taxpayer does not fully reveal. For example, tax agent preference may be driven by the desire not to interact with alternative mechanisms, rather than by any particular added value or benefit from the choice made.
- 4.121 The Committee envisages that the proportion of individual taxpayers with simple tax affairs who continue to use tax agents will reduce as pre-filling reaches a 'push return' situation for many taxpayers. The Committee believes that a taxpayer has a choice in how they complete their return and does not discourage the engagement of tax professionals even for those with standard returns. There is a case, however, for streamlining processes and tax policy so that people do not feel they are obliged to do so.
- 4.122 The Committee considers that, overall, the use of tax agents is a rational decision of individual taxpayers given the current complex tax system,

including the deductions for managing tax affairs, and reducing the use of tax agents should not be an objective of governments or the ATO.

- 4.123 However, the Committee does support the view that if the tax system were to be simplified without compromising other objectives, reduced complexity is expected to reduce the high reliance of taxpayers on tax agents, in particular for those with simple tax affairs.
- 4.124 While policy actions to reduce complexity are beyond the scope of this inquiry and are covered by other inquiries/publications, the Committee notes that reducing complexity is not easily done without consequences for fairness, revenue, or breaking from historical practice, such as allowing claims for workplace related expense deductions. The preceding chapter recommended that a review of the current tax system be undertaken to consider these matters in light of contemporary circumstances.
- 4.125 In support of this measure, and in view of the analysis set out in the final sections of this chapter, the Committee considers that the Australian tax compliance burden could be benchmarked against that in other comparable nations, in order to address the question of what is a reasonable burden and whether policy action should be taken to lower that burden. Any such benchmarking would need to consider tax system complexity as an independent variable.
- 4.126 The Committee 's review suggests that the compliance burden on those individuals who are required to complete a return in Australia is otherwise commensurate with that in many comparable nations, and may be superior to some countries such as the US. However, the comparison does highlight where the Australian compliance burden for tax engagement is high, or could be reduced, based on the number of individuals required to lodge a return.
- 4.127 In this regard, the Committee commends ATO technical initiatives, discussed in Chapter 3, which aim to consolidate Australia's shift to a 'push return' system, allowing taxpayers with consistent tax affairs to approve a prefilled lodgement form.

Recommendation 5

- 4.128 The Committee recommends that the ATO should continue to expand availability of technical initiatives such as pre-filling, simplified electronic lodgement systems for business and individuals, and online**

assessment tools to facilitate Australia's transition to a 'push return' tax system.

While supporting these developments, the Committee upholds the individual's choice to manage their own tax affairs, using ATO or commercial products, and to seek professional advice from tax professionals enabled by efficient online lodgement services.

5. Cash, crime and cards

Introduction

- 5.1 Although the proceeds of crime may be taxed or assets seized, in practice ill-gotten income is rarely captured by the tax system. Super-profits are the incentive for illegal trade and as such the business model is to avoid contact with government authorities. Operations are set-up to disengage from formal reporting systems. As such, determining mechanisms to reduce the tax gap from criminal operations is fraught—and it is counter-intuitive to attempt to do this through taxpayer engagement measures.
- 5.2 Theoretically, social acceptance of cash economy activity could also be counteracted by employing behavioural insights to promote moral and ethical behaviour in the community. These issues are explored by the Government's Black Economy Taskforce, which provides a background and context for the Committee's evaluation of revenue loss to the cash economy and the ATO's programs to address it.
- 5.3 As the Taskforce noted in its Interim Report: 'The black economy is not simply a tax phenomenon'. However, a simple definition clarifies the relationship between it, and the impact of cash activity on tax revenue:
 - ...the black economy refers to businesses and individuals who operate outside the tax and regulatory system. Other terms used include: the shadow economy, cash economy and underground economy. Businesses and individuals may entirely avoid reporting activities, or they may deliberately

underreport income in order to evade their obligations. The activities themselves would otherwise be legal, but there may be complex linkages with illegal activities (for example, money laundering).¹

Definition of the cash economy

- 5.4 The OECD defines the term tax evasion as ‘illegal arrangements where liability to tax is hidden or ignored’.² This contrasts with tax avoidance, which is described as an ‘arrangement of a taxpayer’s affairs that is intended to reduce his liability and that although the arrangement could be strictly legal, it is usually in contradiction with the intent of the law it purports to follow’.³ Hence, tax evasion is illegal, while tax avoidance (strictly speaking) is legal.
- 5.5 Tax evasion includes the operation, or partial operation of a business in cash transactions which are not declared in the tax system. It is important to emphasise that a cash payment is legal tender and trading in cash is no less authentic or legitimate than electronically generated payments.⁴ It does, however, (in most cases⁵) require non-automated recognition of the receipt of such money to be tax compliant. This is where cash-only or cash dominant businesses may fall short of their tax obligations, whether deliberately or unintentionally.
- 5.6 Cash dominant businesses are vulnerable to tax evasion practices because such a business environment offers greater opportunities for businesses and individuals to avoid tax and superannuation obligations. This can occur through:

¹ The Australian Government, The Treasury, *Black Economy Taskforce Interim Report*, March 2017, p. 11.

² Tax ‘Evasion’, OECD, *Glossary of Tax Terms*, <www.oecd.org/ctp/glossaryoftaxterms.htm> viewed 20 December 2017.

³ Tax ‘Avoidance’, OECD, *Glossary of Tax Terms*, and see ATO, ‘Tax Crime Explained’ <www.ato.gov.au/general/the-fight-against-tax-crime/tax-crime-explained/> viewed 20 December 2017.

⁴ Noting, however, that the Government announced in the 2018-19 Federal Budget the implementation of the recommendations detailed in the Black Economy Taskforce Final Report—October 2017 (May 2018) which included outlawing cash payments in excess of \$10 000.

⁵ Some cash operations are automatically recognised at point-of-sale. For example, cash accepting parking booths.

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- Under declaring income or sales;
 - Failing to provide regulated obligations to employees including—
 - Underpaying wages *or* paying wages in cash with employee ‘off the books’,
 - Failing to withhold tax and failing to meet superannuation obligations.
 - Individuals receiving social welfare benefits with no entitlement.⁶
- 5.7 Businesses trading in legal products and services may not be fully declaring their cash income, and some not at all. This is where the tax administration focus of re-engagement lies.
- 5.8 As a by-product of such focus, criminal activity may be revealed—especially where ‘front’ or parallel businesses are used to wash or launder money through a legitimate business. The ATO works collaboratively with enforcement bodies and intelligence agencies, such as the Australian Federal Police, Australian Crime Intelligence Commission and the Australian Transaction Reports and Analysis Centre (AUSTRAC), to identify and prosecute this tax evasion. The tax administrator’s primary focus is however is on educating those in legal trade about their obligations and capturing the proceeds of legitimate business activity, including where individuals and businesses partially comply.
- 5.9 Support for further collaboration, data sharing and advanced analytics between agencies; and undertaking a public awareness campaign about the risks of operating in the black economy and positive social norms were recommended in the Black Economy Taskforce Final Report and announced in the 2018–19 Budget.⁷
- 5.10 Criminals have a business model of non-engagement and behavioural insights and penalties are unlikely to induce them to declare income which would implicate them in criminal activity. The ATO has recently stated in a submission to the Committee’s 2016–17 ATO annual report performance review that its focus for addressing the cash and hidden economy is through ‘...protecting honest businesses from unfair competition’.⁸

⁶ Australian Taxation Office (ATO), *Submission 2*, Inquiry into the 2016–17 Annual Report of the ATO, p. 10.

⁷ The Australian Government, The Treasury, *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 6.

⁸ ATO, *Submission 2*, Inquiry into the 2016–17 Annual Report of the ATO, p. 10.

- 5.11 The focus of the Committee’s inquiry on engagement in the cash economy is therefore on tax evasion through undeclared or under-declared cash income in the legal economy. There is also some consideration of evidence which relates to the nexus between undeclared cash or illicit business activity, its impact on compliant businesses, and criminal tax evasion, including the capacity to launder money through the use of global payment technologies.

The size of the problem

- 5.12 Estimates of revenue loss associated with the cash economy are made as a proportion of the total estimated tax gap, which is in itself a conjectural exercise.
- 5.13 For example, the Government’s *Black Economy Taskforce Interim Report* (March 2017) stated that: ‘The Australian Bureau of Statistics (ABS) estimated in 2012 that the black economy had grown to 1.5 per cent of GDP (\$25 billion per year in today’s dollars) in Australia’.⁹ The Taskforce’s final report (May 2018) stated that the 2012 estimate relied on data dating back as far as 2001, and recent ABS estimates suggest the black economy as a proportion of GDP has doubled—to three percent, or approximately \$50 billion per year.¹⁰
- 5.14 As for the revenue lost, the Australian National Audit Office (ANAO) reported in 2006:

The ATO does not attempt to estimate the size of the ‘cash economy tax gap’ (the gap attributed to the use of cash and not declaring income). The ATO reasons, having also considered overseas practice in measuring the tax gap, that accurate and defensible measures of the tax gap are impossible to achieve in a practical sense. It considers that the time, cost and the intrusive burden on taxpayers imposed by an exhaustive exercise rule out conducting such an estimate.¹¹

- 5.15 However, the ATO has more recently made commitments to better understand and evaluate the cash related tax gap as part of its broader tax gap analysis, advising in March 2017, that:

⁹ The Australian Government, The Treasury, *Black Economy Taskforce Interim Report*, March 2017, p. 11.

¹⁰ *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 23.

¹¹ Australian National Audit Office (ANAO), *The ATO’s Strategies to Address the Cash Economy*, February 2006 <www.anao.gov.au/work/performance-audit/atos-strategies-address-cash-economy> viewed 10 March 2018.

... We do not yet have any new estimate around the cash economy. We anticipate that, by the end of this calendar year or thereabouts, we should have an estimate across all income tax. That should give us a bit of a steer about the cash economy as well. Exactly how much of a steer is yet to be seen as that work unfolds, but we are hopeful of having an initial indication as we complete our work over the course of this calendar year. In the meantime, as you would be aware, there are estimates from the Australian Bureau of Statistics of the overall size of the unobserved economy—as they call it—and that is the best information we have at the moment.¹²

Measurement in other countries

5.16 The Inspector-General of Taxation's submission noted that the ATO's recent tax gap assessment methodology aligns with that adopted by Her Majesty's Revenue and Customs (HMRC) in the United Kingdom (UK).¹³

5.17 The HMRC provides an annual estimation of the size of the UK tax gap, which it describes as 'the difference between the amount of tax that should, in theory, be collected by HMRC, and what is actually collected'.¹⁴ The HMRC's *Measuring Tax Gaps 2017* report advised its tax gap estimate for 2015–16 period was £3.5 billion or 6 per cent of the total theoretical tax liabilities, with the caveat that:

We use a range of internal and external data and different analytical techniques to produce annual estimates, which we revise as more accurate data becomes available. These are our best estimates based on the information available, but there are many sources of uncertainty and potential error.¹⁵

5.18 These uncertainties are indicative of the HMRC's data estimates for the hidden economy.¹⁶ For the 2015–16 financial year the HMRC estimated that

¹²Mr Neil Olesen, Second Commissioner ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 2.

¹³ Inspector-General of Taxation (IGT), *Submission 5*, p. 6

¹⁴ HM Revenue and Customs (HMRC), *Measuring Tax Gaps 2017 Edition, Tax Gap Estimates for 2015–16*, Official Statistics released 2017, p. 3.
<www.gov.uk/government/uploads/system/uploads/attachment_data/file/655097/HMRC-measuring-tax-gaps-2017.pdf> viewed 10 March 2018.

¹⁵ HMRC, *Measuring Tax Gaps 2017 Edition, Tax Gap Estimates for 2015–16*, Official Statistics released 2017, p. 3.

¹⁶ The Oxford dictionary defines the *hidden economy* as 'the economic sector consisting of transactions that are (illegally) not declared for tax purposes, and which are therefore not taken into account

the tax gap attributable to the hidden economy was £1.7 billion.¹⁷ In 2017, the HRMC was able to report that, due to refinements in its survey and assessment methods:¹⁸

The hidden economy tax gap has been revised down by £2.7 billion due to more accurate data being available. Fewer people are operating in the hidden economy than we estimated previously and their average incomes are lower.¹⁹

Where is cash activity concentrated?

5.19 The ATO uses risk-based approaches to identify taxpayers or transactions which it considers represent a higher risk of non-compliance. It currently publishes material about specific industries in which it is seeing disproportionate numbers of businesses that:

- indicate unrealistic income relative to the assets and lifestyle of the business and owner;
- fail to register for GST or lodge activity statements or tax returns;
- underreport transactions and income according to third-party data;
- fail to meet super or employer obligations;
- operate outside the normal small business benchmarks for their industry; or
- are reported to the ATO by the community for potential tax evasion.²⁰

5.20 Commensurate with the focus of the current inquiry, it is important to note that small business is a longstanding focus of ATO activities in combatting the black or cash economy.²¹

in official statistics'. <en.oxforddictionaries.com/definition/hidden_economy> viewed 7 February 2018.

¹⁷ IGT, *Submission 5*, p. 6.

¹⁸ In particular, a new distinction was made between two elements: 'ghosts' and 'moonlighters'. The HRMC Report 2017 advises that: 'Ghosts are individuals whose entire income is unknown to HMRC, while moonlighters are individuals who are employees and pay tax on the earnings from their main job through PAYE, but have other undeclared sources of income'. See HRMC, *Measuring Tax Gaps, 2017* edn, pp. 63, 68.

¹⁹ HRMC, *Measuring Tax Gaps, 2017* edn, p. 11.

²⁰ IGT, *Submission 5*, p. 10.

²¹ *Black Economy Taskforce Interim Report*, March 2017, p. 25.

- 5.21 The Committee asked Second Commissioner Neil Olesen for clarification of the distinction between criminal tax evasion and the ATO's work on undeclared income or cash:

Whilst clearly there is criminal activity in Australia that is funded by cash, I would not pretend that most of the hidden economy in Australia is because of that. There is a lot of cash economy activity where people that run coffee shops, hairdressers or beauty salons are not paying tax on their cash. Generally they are relatively small amounts, but in other parts of the economy the picture is different.²²

- 5.22 The ATO's Ms Emma Rosenzweig, Acting Deputy Commissioner, Small Business, advised that there are approximately 1.6 million businesses at high risk for cash economy behaviour, with the three highest risk industries being building and construction; restaurants, cafes, takeaways and personal services, and hair and beauty operations. However, she qualified this advice, saying: 'We do not think 1.6 million businesses are operating in the cash economy; we think there are 1.6 million businesses in those industries that are of highest risk of cash economy like behaviours'.²³

- 5.23 As the Black Economy Taskforce has noted, the impacts and drivers of black economy activity are multiple, and include policy, regulatory settings—such as small business regulatory frameworks; welfare and immigration policy settings; the role of cash in the payment system; the verification of business and individual identities; as well as the links with illegal activities, such as money laundering.²⁴

- 5.24 Activities associated with the black economy are thus not just associated with projected revenue loss, as damaging as this is, but also with the broader destabilisation of economic activity and perceptions of the fairness or unfairness of the tax system in the taxpaying community, which may in turn drive cash economy activity.

- 5.25 The Black Economy Task Force interim report explained:

Black economy activities undermine the community's trust in the tax system; create an unfair commercial environment which penalises businesses and individuals doing the right thing; enable and entrench the exploitation of

²² Mr Olesen, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 2.

²³ Ms Emma Rosenzweig, Acting Deputy Commissioner, Small Business, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 10.

²⁴ *Black Economy Taskforce Interim Report*, March 2017, p. 2.

vulnerable workers; undermine tax revenue; and enable abuse of the welfare system. If unchecked, increasing black economy participation can lead to a dangerous dynamic. It can foster a culture which legitimises and supports this participation, spurring its further growth. As revenues fall, those remaining in the formal economy may ultimately be faced with higher tax burdens, giving them a greater incentive to move into the shadows.²⁵

The ATO's cash economy measures

- 5.26 The ATO has a suite of measures to combat the undeclared cash economy. These range at the front end from community education and awareness to data matching, industry yardsticks and supporting the community to report tax cheats, to back end enforcement including penalties and prosecution for serious tax evasion cases.²⁶
- 5.27 As discussed in Chapter 2, revenue agencies and governments around the world have also focused on digitisation of their taxation systems along with other strategies to monitor and minimise domestic cash activity and to educate the community about the impacts of such activity. They have also endorsed information sharing agreements, such as the Common Reporting Standard (CRS) and global tax initiatives such as the Base Erosion and Profit Shifting (BEPS) project to close gaps in revenue associated with serious tax avoidance.
- 5.28 The ANAO's review of the ATO's strategies and activities to address the cash and hidden economy (2015–16), concluded that its methods were on par with international approaches and guidelines provided by the OECD. It also considered the ATO's planning, liaison and reporting arrangements had been sound, and its risk management activities cost effective.²⁷
- 5.29 The review referred to ATO advice that, over 2015–16, the revenue agency had committed approximately 400 staff and a budget of \$39.5 million to combat the risk posed by the cash economy. The report also noted that in the four previous years from 2011–12 to 2014–15, the average annual liabilities raised by the ATO from compliance activities with small business taxpayers

²⁵*Black Economy Taskforce Interim Report*, March 2017, p. 1.

²⁶ ATO, *Submission 15*, pp. 9–10.

²⁷ ANAO, *Strategies and Activities to Address the Cash and Hidden Economy*, ATO, *Performance Report 2015-16*, no. 27, p. 7.

to address the cash economy was \$192.6 million, and an average annual of \$114 million cash was collected.²⁸

5.30 The submission from the ATO further advised the Committee, that:

In 2015–2016 the ATO contacted over 127 000 businesses exposed to the cash and hidden economy. Approximately 13 500 compliance activities were conducted, resulting in more than \$208 million in tax and penalties raised from businesses engaged in unfair competition. In the first six months of 2016–2017, the ATO has undertaken over 17 000 activities and raised more than \$107 million in tax and penalties.²⁹

Role of data analytics

5.31 As discussed previously in this report, advanced data analysis is being conducted in a number of jurisdictions to better identify areas of high risk for cash economy activity and revenues evasion, including where this intersects with criminal activity. Jurisdictions have also adopted a range of methodologies to assess the size of the tax gap associated with cash activity, with some attempting an estimate of losses associated with tax-related illicit activity, such as through money laundering.

5.32 Over the last decade advances in data collection, analysis and dispersal at revenue and partner agency level has become the norm in most comparable jurisdictions. Huge improvements in data storage and management capacity have enabled sophisticated algorithms to assess and crossmatch information recorded in large data sets to detect anomalies.³⁰

5.33 In recent years, the ATO has deployed computerised risk models and specific data matching capacities using information from other agencies to target its compliance activities.³¹ The ATO's submission reports that it now collects information from a wide range of third-party sources, both public and private, with more than 600 million transactions reported to it annually.³² These data sources include investment income information from banks, financial institutions and investment bodies, employment

²⁸ ANAO, *Strategies and Activities to Address the Cash and Hidden Economy*, ATO, *Performance Report 2015–16*, no. 27, p. 7.

²⁹ ATO, *Submission 15*, p. 18.

³⁰ OECD, *Tax Administration 2017, Summary*, p. 1.

³¹ Referred to in IGT, *Submission 5*, p. 10.

³² ATO, *Submission 15*, p. 9.

information and on welfare payments. The supply of this data is authorised by law. The data is matched with ATO gathered information to detect those who may not be correctly disclosing all of their income.³³

- 5.34 AUSTRAC advised of its role in data collation and matching as a key data source for monitoring of tax evasion. As noted in Chapter 2, AUSTRAC leads in sharing information online to all its partner agencies, compared with similar agencies in other countries around the world. Mr David Hawkins, Acting National Manager, Strategic Intelligence and Policy, advised that:

There are some 3 000 to 4 000 government officers, state and federal government, that have online access to the database. They are doing their own investigations and are drawing on the intelligence. It is not just AUSTRAC pushing this out. There is a lot of intelligence being gathered directly from the database, from the partner agencies.³⁴

- 5.35 It was speculated that sophisticated data-matching capability and data analytics by the ATO, particularly with access to taxpayers' banking records, and, potentially, their payments transactions through the New Payments Platform (NPP), may contribute to tackling the cash economy.³⁵
- 5.36 Dr Anthony Richards, Head of the Payments Policy Department, Reserve Bank of Australia (RBA) highlighted the progress that has been made towards real-time processing in the banking sector:

Well, it was not that long ago that if I wanted to make you a payment, I could go on to mybank's app. The payment message from my bank to your bank would not be exchanged today [Friday]. I think it would have been exchanged on early Monday morning. Then your bank would at some point subsequently post that money to your account. You might see it sometime on Monday. More recently, we have got what is called same day settlement in the payments system, which means that if I send you some money now, you will probably see it in about three hours in your account. There is now a new set of rails that will enable banks to make those payment instructions in real time. They just

³³ ATO, 'Tax Crime Explained', 24 November 2017.

³⁴ Mr David Hawkins, Acting National Manager, Strategic Intelligence and Policy, Australian Transaction Reports and Analysis Centre (AUSTRAC), *Committee Hansard*, Canberra, 21 June 2017, p. 5.

³⁵ Tax and Super Australia, *Submission 12*, p. 4.

have not had that set of rails that enable real-time payment instructions to go between them. That is the real innovation.³⁶

- 5.37 However, the ATO's Chief Digital Officer and Deputy Commissioner John Dardo cautioned that there are currently limitations that would curtail tracking of such personal information, even if there was the technological facility to do so. Commenting on the NNP, he observed:

We see that the NPP will be able to facilitate interactions. The overlay services that sit over the top of that and/or the identity requirements that sit in it are something for government and/or industry to really work through. I imagine that there will be a range of discussions about what may or may not sit in the NPP. Certainly if a bank chose to use the NPP to create an overlay service for that bank or that bank's customers allowed them to do a whole bunch of really interesting stuff, such as codifying at point of sale the gross versus GST and offering that as a service so that bank could say, 'Well, if you use this type of account with us, you actually do not need to run a separate reporting or recording system and we will import that straight in', that is cool. But I do not think we are at the point where things are being mandated for the NPP either on an identity front or on the reporting front.³⁷

Supporting Honest Business Program

- 5.38 The ATO released its new targeted cash economy initiative, the Supporting Honest Business Program (SHBP), part-way through the Committee's inquiry in June 2017.³⁸ The model demonstrates the utility of data analysis to design and co-ordinate integrated strategies, from provision of information through to targeted enforcement to improve compliance.
- 5.39 Sophisticated data analysis is first used to pinpoint regional anomalies (giving economies of scale in field visits and aiming to influence a wider group of small business). The information is used to locate sessions with both traders and the tax professionals in the targeted region, and then follow up on-site compliance visits, for further education and opportunities for voluntary disclosure. These visits also provided a catalyst for reporting on

³⁶ Dr Anthony Richards, Head, Payments Policy Department, Reserve Bank of Australia (RBA), *Committee Hansard*, Canberra, 27 October 2017, pp. 31–32.

³⁷ Deputy Commissioner Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 5.

³⁸ ATO, *Commissioner of Taxation Annual Report 2016–17*, pp. 29, 30, and see Supporting Honest Business Program (SHBP) in ATO, *Inquiry into the ATO Annual Report 2016–17 review, Submission 2*, p. 10.

local competitors known to be habitually dodging their tax and employer obligations.³⁹

5.40 The precursor to this program was the ATO's 'Working with Industry' campaign which focused on specific cash dominant service sectors, such as hair and beauty, and restaurants and cafes. The 'Working with Industry' campaign led to a five per cent increase in on-time tax lodgements for businesses visited. Importantly, there was also a three per cent compliance flow-on effect in other businesses in the sector. The ATO advised that the follow-up education campaign flushed out a 34 per cent increase in reports to the Tax Evasion Reporting Centre for the hair and beauty industry.⁴⁰

5.41 The model has synergies with those currently deployed in a number of other jurisdictions. The Inspector-General of Taxation cited developments in New Zealand and the United Kingdom:

- In New Zealand, the Inland Revenue Department (IRD) had indicated in 2011 that it had adopted a range of strategies to target different industries in which higher risk had been identified. These strategies included raising awareness of obligations, enforcing penalties, prosecuting serious offenders, increasing data matching and partnering with industry associations and other government agencies on education, information sharing and investigations.
- In 2016, the HMRC published a number of consultation papers in relation to proposals to assist in tackling the cash economy...The current proposed strategies are three-pronged and include extending the data-gathering powers to 'money service businesses', the need for new penalties and sanctions as well as conditional registration. The latter point requires 'tax registration as a condition of access to some essential business services or licences'. As part of its strategy the HMRC is also seeking to identify points at which businesses tend to enter the cash economy by failing to register for certain taxes (such as Value Added Tax when certain thresholds are met) and making it as easy as possible for taxpayers to register.⁴¹

³⁹ ATO, Inquiry into the ATO Annual Report 2016–17 review, *Submission 2*, p. 10.

⁴⁰ Including from compliant competitor businesses in the industry, ATO, *Submission 2*, Inquiry into the 2016-17 Annual Report of the ATO, p. 12.

⁴¹ IGT, *Submission 5*, pp. 8–9.

Cash, crime and corporate fraud

- 5.42 It has been considered that the difference between tax planning and tax avoidance largely comes down to intent. Tax planning is organising your clients' tax affairs in the most tax effective way within the intent of the law. In contrast, tax avoidance schemes involve the deliberate exploitation of the tax system.⁴²
- 5.43 Tax crime advances by degrees to culminate in the individual or business involved deliberately abusing the tax and super systems for financial benefit. Crimes range from hiding cash income or wages to avoid payment or tax obligations, to using complex offshore secrecy arrangements to falsely claim refunds and benefits one is not entitled to.⁴³
- 5.44 As already noted in this chapter, revenue agencies in different nations take different positions on whether or not illicit or illegal activities contributing to, or associated with, tax avoidance or fraud are included in estimates of a nation's revenue gap.
- 5.45 The ATO's Mr Olesen indicated that this is understandably a very difficult area for assessment. However, he undertook to investigate what had been done in the area, advising of the expected release of work, referred to above, being done on tax gap analysis more broadly.⁴⁴
- 5.46 Mr Olesen also explained how the ATO's cash economy audits had identified key sectors of concern for cash activity, and the nexus between the ATO's work on under reportage and its surveillance of criminal tax evasion with partner agencies:

Those conclusions that we have given you now are not drawn from the gap analysis, because we do not have a final gap analysis. We are in the process of doing some of the random activity that we need to do to get the datasets that allow us to make the estimates. Instead, what I am drawing on is all the work we have done in the field, year after year, doing audits and reviews of cafes and restaurants, and the work that we do at the criminal end of things as well,

⁴² ATO, Tax Planning vs Tax Avoidance <www.ato.gov.au/General/Tax-planning/Tax-planning-vs-tax-avoidance/> viewed 20 December 2017.

⁴³ ATO, 'Tax Crime Explained', viewed 20 December 2017.

⁴⁴ ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 12.

where we also work closely with our colleagues in the Federal Police and the Crime Commission.⁴⁵

Cash under the counter

- 5.47 As noted above, the ATO has recently stepped up surveillance of identified businesses for the risk of cash activity under its Supporting Honest Business Program (SHBP).⁴⁶
- 5.48 According to its most recent advice, the ATO's increased visibility in the community—with over 1 200 business visits—resulted in \$6.6 million in tax and penalties raised.⁴⁷ As a result of this success, the program was expanded across all industries. The SHBP comprises:
- Data analysis using industry norms and cross-matching with third-party data to identify regions with high levels of cash-dominant businesses;⁴⁸
 - Writing to identified businesses and tax practitioners in that region and inviting them to an information session (correspondence available in a variety of languages); and
 - Follow-up site visits to vulnerable businesses (known as the 'cash only visits') to provide tailored education and assistance.⁴⁹
- 5.49 The business visits in the SHBP have revealed that many businesses are not meeting record keeping obligations—some due to deliberate tax evasion and others from record processing ignorance.⁵⁰ There are also businesses not

⁴⁵ Mr Olesen, ATO, *Committee Hansard*, Canberra, 29 March 2017, pp. 9–10.

⁴⁶ ATO, *Commissioner of Taxation Annual Report 2016–17*, pp. 29, 30, and see Supporting Honest Business Program (SHBP) in ATO, *Inquiry into the ATO Annual Report 2016–17 review, Submission 2*, p. 10.

⁴⁷ ATO, *Submission 2, Inquiry into the 2016-17 Annual Report of the ATO*, p. 10.

⁴⁸ Regions with a high proportion of cash-only businesses included in the 2 600 site visits since June 2017 included Cabramatta and Liverpool in NSW, Werribee and Glen Waverley in Victoria, Sunnybank in Queensland and Glenelg in South Australia. The program will include in 2018 Mandurah in Western Australia, Batemans' Bay, inner metro Sydney and Chatswood in NSW, metro Melbourne in Victoria, Toowoomba and Cairns in Queensland and Western Adelaide, South Australia.

⁴⁹ Around 60 per cent of these businesses are subject to follow-up activity from record keeping workshops, electronic payment options through to voluntary disclosure of errors or omissions before an audit proceeds.

⁵⁰ Those exhibiting ignorance are given record-keeping support in the field and through record-keeping workshops. ATO, *Submission 2, Inquiry into the 2016-17 Annual Report of the ATO*, p. 12.

appropriately recording (or not recording all) their sales and some without a current Australian Business Number (ABN) and/or GST business registrations. In addition, there was an across-the-board misunderstanding of employer obligations which included not paying superannuation or registering for Pay As You Go (PAYG) withholding tax and reports of cash wages.

5.50 The Committee heard evidence of the impact of deliberate evasion activity on legitimate businesses in the grocery and tobacco retail sector, and its projected nexus with the illegal tobacco trade.

5.51 Mr Jos de Bruin, Chief Executive Officer of the Master Grocers Australia (MGA) spoke of the prevalence of under-the-counter sales of tobacco and online sales of illicit tobacco, and its impact on compliant small businesses:

It does have that knock-on effect, for sure. You know this but when we are running legitimate businesses, complying with everything that we need to comply with, and there are illegitimate sales outside of our shops then there is going to be an economic effect of some kind because you gear your business up to a certain level of business and if that business is not coming in you have to readjust.⁵¹

5.52 Mr de Bruin further reported on the impact of criminal activities associated with this illicit trade, including robberies of grocery stores, which indicated a need for increased powers for enforcement against this illicit trading at the local level.⁵² While his evidence in part reflected industry concerns about the high taxes imposed in Australia on tobacco and the imputed knock on effects, Mr Rohan Pike, Illicit Trade Adviser of the Australian Retailers Association (ARA) also highlighted broader problems for customs and border protection officials in vetting legitimate imports of products, and for the Tax Office in monitoring and collecting excise on tobacco.⁵³

5.53 Dr Craig Latham, Deputy Australian Small Business and Family Enterprise Ombudsman, brought the focus back to fairness in tax law and administration for any small businesses which may be tempted to engage in cash-based trade:

⁵¹ Mr Jos de Bruin, Chief Executive Officer, Master Grocers Australia (MGA) *Committee Hansard*, Canberra, 25 October 2017, p. 4.

⁵² Mr de Bruin, MGA, *Committee Hansard*, Canberra, 25 October 2017, pp. 5, 3.

⁵³ Mr Rohan Pike, Illicit Trade Adviser, Australian Retailers Association (ARA), *Committee Hansard*, Canberra, 25 October 2017, p. 11.

Certainly having a healthy small business sector that's not under pressure would be fundamental to improving the cash economy, in any case. Alongside that, I mentioned before that a good tax system includes good policy plus administration, so it's again crafting regulation that has small business in mind. When we do changes, the person who runs the small business is the person who's on the floor, who does the compliance activities, so having that person in mind whenever you do a change around policy or administration is critically important.⁵⁴

Associations with money laundering

5.54 During the course of the inquiry there was discussion of the relationship between cash activity conducted by a business and the potential for this money to be laundered to avoid detection. These moneys might support a personal lifestyle, such as in purchasing high value goods or enable criminal, or even terrorist, activity in Australia or overseas.

5.55 While these concerns may appear at the periphery of the Committee's focus on tax engagement with the individual and small business sectors, evidence suggested otherwise. The Attorney-General's submission advised, for example, of Australian Criminal Intelligence Commission findings that:

...the construction industry provides considerable scope to launder money, for example, via paying tradespeople in unrecorded cash for part of their work or paying for part of the cost of materials in unrecorded cash. This in turn causes the cost of construction and renovations to be understated so that an artificially large profit will be created.⁵⁵

5.56 Moreover, the Attorney-General's submission advised that commonly used corporate organisation structures can facilitate large scale money laundering by criminals in Australia:

Organised criminals also exploit the Australian taxation system by using increasingly complex and sophisticated organisational structures – making these entities less recognisable and harder to detect. ACIC intelligence suggests that organised criminals are commonly using one of Australia's most common forms of business structure, the sole trader (which makes up the highest proportion of registered businesses in the country), to facilitate illicit activity. This type of structure is predominantly used to operate businesses in

⁵⁴ Dr Craig Latham, Deputy, Australian Small Business and Family Enterprise Ombudsman, *Committee Hansard*, Canberra, 13 September 2017, p. 6.

⁵⁵ AGD, *Submission 13*, p. 6.

cash-intensive industries, and these industries are attractive to organised crime because of the relatively untraceable nature of cash transactions and the opportunities to commingle illicit and legitimate funds. Organised crime groups can create multiple sole trader entities in order to facilitate tax evasion or money laundering activities.⁵⁶

- 5.57 The recommendation of the Black Economy Taskforce to outlaw cash payments in excess of \$10 000 was designed to ameliorate the channelling of cash proceeds into money laundering activity or the purchase of high value goods with undeclared cash income.⁵⁷
- 5.58 Another potential avenue for money launderers was the transferal of moneys undetected using electronic payment platforms in the global payments market. Ms Jasmine Koh, General Counsel to Airwallex, a global payment fintech, emphasised the importance of her firm’s strict observance of Australia’s Anti-Money Laundering and Counter-Terrorism Financing AML/CTF framework for security and compliance.⁵⁸
- 5.59 While approving Australia’s regime, Ms Koh noted that in some other countries, such as Singapore, the legal frameworks are still evolving.⁵⁹ This poses as a challenge for payment platforms in vetting transactions and complying with all overseas AML regimes as real-time transactions are facilitated by the NNP:

In terms of the new payments platform, the attraction of the NPP is that it is going to be in real time or near real time. Because of that shortage of time, what happens is that we don’t have as much time to conduct the necessary KYC [Know Your Client] checks that are required by the AML legislation. Yes, the benefit is that your beneficiary gets payments pretty quickly, but, at the same time, if there were a red flag—for example, if there were a company that had politically exposed persons employed or sitting on their board of directors—usually what would happen is we would do a further check into the company to see if there were going to be any risks. In certain countries where you have politically exposed persons there might be a higher risk of laundered money going through the system, or there might be funds which are the proceeds of tax avoidance. The NPP, while good in terms of real-time settlements, won’t give us that necessary time to figure out if the funds that

⁵⁶ AGD, *Submission 13*, p. 6.

⁵⁷ *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 51.

⁵⁸ Ms Koh, Airwallex, *Committee Hansard*, Melbourne, 18 July 2017, p. 17.

⁵⁹ Ms Koh, Airwallex, *Committee Hansard*, Melbourne, 18 July 2017, p. 17.

are being channelled into Australia, for example, would be dirty money, for want of a better term. So it is that balance.⁶⁰

- 5.60 In an interview, Ms Koh emphasised that compliance with the AML is ‘not a singular operation’ but ‘a joint effort’ between all partners involved to ‘apportionment of duties and responsibilities for compliance with AML’.⁶¹
- 5.61 During the period of this review, the Government introduced the Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2017 (the Bill).⁶² The Bill aimed to address 19 of the review recommendations with the objective, among other things, of establishing a more flexible and effective framework for sharing AUSTRAC information, improving identity credentials, including with the private sector, and expanding the powers available for investigations and enforcement related to the regulatory regime.⁶³ The Bill was passed and assented to in late December 2017.⁶⁴

Corporate regulation

- 5.62 As noted above, corporate regulatory structures and rules have the capacity to open up loop holes which support tax avoidance, with negative effects for whole industry sectors and deep impacts on the ATO’s revenue collection. The Inspector-General of Taxation’s submission advised of strategies proposed in 1998 by the then government, based on the finding that ‘taxes and collection systems allow too much scope for taxpayers to participate in the cash economy’. These included the introduction of the Australian Business Number (ABN) as a single business identifier, simplifying payment

⁶⁰ Ms Koh, Airwallex, *Committee Hansard*, Melbourne, 18 July 2017, p. 15.

⁶¹ In background material provide to the Committee, J Hailstone, ‘Talking to Airwallex: Jasmine Koh’, 14 June 2017.

⁶² On 17 August 2017, see Federal Legislation <www.legislation.gov.au/Details/C2017B00166> viewed 5 December 2017.

⁶³ Which contained the first set of amendments resulting from a statutory review of the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (AML/CTF Act) and related Regulations and rules that was completed by the AGD in 2016. Information on the AML/CTF drawn from the Parliamentary Library Bills Digest no. 47, 2017–18, 25 October 2017, and the AGD, *Submission 13*, p. 7.

⁶⁴ Assented Act no 130, 2017, 13 December 2017, see Parliamentary Business, Australian Parliament House, Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2017 <www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bId=r5952> viewed 19 April 2018.

and reporting systems (the PAYG system) as well as other law and administrative changes to promote certainty and make compliance simpler and fairer.⁶⁵

- 5.63 Evidence to the inquiry discussed the limitations of the business registration systems in the context of their potential to contribute to non-complaint behaviours and tax avoidance.

Business registration and PAYG

- 5.64 The introduction of ABNs was expected to disadvantage unregistered businesses that would have a significant proportion of their payment withheld by trade partners and remitted to the ATO.⁶⁶ However, the Committee heard the regime has a number of deficiencies.

- 5.65 The Institute of Public Accounts (IPA) maintained:

When the Australian Business Number (ABN) was introduced, it was intended to make significant inroads into the cash economy. Unfortunately the ABN system has not been an effective mechanism for dealing with this sector. There are a significant number of ABNs against where there has been no business activity recorded. There is also widespread practice of quoting invalid or some other entities' ABN details. ABN holders are excluded from the PAYG withholding system unlike employees earning salary and wages. The system requires the paying entity to check the ABN details of the service provider. If this is not done properly, it is relatively easy for an entity to use an invalid ABN or use someone else's ABN details so the veracity of the existing system relies very much on this process. The current system requires businesses to self-assess their PAYG income tax instalments on the basis that they are going to declare all their income in their tax returns. There is only one industry sector that requires reporting of payments made to contractors to enable the ATO to perform a data cross check. Apart from this there is no data matching mechanism to ensure that all invoices have been included in the taxpayer's income tax return.⁶⁷

- 5.66 Mr Peter Strong, CEO of the Council of Small Business Australia, agreed that more needed to be done to verify businesses registering for an ABN, considering that the current approach has 'made it too easy to get an ABN'. Nevertheless, he cautioned Government not to make the bar too high,

⁶⁵ IGT, *Submission 5*, p. 9.

⁶⁶ IGT, *Submission 5*, p. 9.

⁶⁷ IPA, *Submission 2*, p. 4

referring to deliberations in the Black Economy Taskforce's interim report on the potential to introduce an Australian Business Licence qualification for all entrepreneurs wanting to register a business.⁶⁸

Phoenix activity—director identification

5.67 Phoenix activity is the creation of a new business to continue the activities of another business that was deliberately shut down leaving debts, which could include tax, creditors and employee entitlements. While this activity goes beyond strict tax compliance, these activities have heavily impacted compliance with tax laws.

5.68 The submission from Professor Helen Anderson of Melbourne Law School, University of Melbourne, made the distinction between legal and illegal phoenix activity:

Legal phoenix activity occurs when the previous controllers of a usually failed business, start another similar business, using a new company usually in order to rescue its business. Illegal phoenix activity on the other hand involves similar activities, *but the intention* of the phoenixing is to exploit the corporate form such that unsecured creditors, including the tax administrator and employees are never paid. The illegality rests with a breach of directors' duties in failing to act properly in respect of the failed company and its creditors.⁶⁹

5.69 Professor Anderson maintained that phoenix activity, if left unchecked, 'has the capacity to undermine Australia's revenue base and the competitive 'level playing field'.⁷⁰ She recommended introducing a director identification number such that:

- All existing and new directors should be required to have a director identification number ('DIN'), issued for a small charge that would allow ASIC and other regulators to accurately track repeat players.
- This would eliminate fictitious directors, or directors incorporating companies with their own name misspelt or a false date of birth, or naming unconnected people as directors without their consent.⁷¹

⁶⁸ Mr Peter Strong, CEO, Council of Small Business Australia, *Committee Hansard*, Canberra, 16 August 2017, p. 18.

⁶⁹ Prof Helen Anderson, *Submission 23*, p. 1.

⁷⁰ Prof Helen Anderson, *Submission 23*, p. 1.

⁷¹ Prof Helen Anderson, *Submission 23*, p. 2.

5.70 The Government is currently considering introduction of legislation to require registration of Directors Identification Numbers (DIN), a measure strongly supported by Professor Anderson's research. The ATO outlined the progress on the DIN regime in its supplementary submission:

On 28 September 2017, the Treasury released a consultation paper on reforms to Address Illegal Phoenix Activity, with comments closing on 27 October 2017. The Treasury discussion paper was informed by input from the Serious Financial Crime Taskforce, the Phoenix Taskforce and the Black Economy Taskforce. The ATO is a member of each of these taskforces and believe that the various proposals in the Treasury discussion paper could contribute to the reduction in illegal phoenix activity.

The ATO has consulted with the Australian Securities and Investment Commission (ASIC), the DTA and other agencies, including the Department of Employment in relation to the Fair Entitlement Guarantee about how a DIN, if implemented, could deter illegal phoenix activity and provide better outcomes for the community.⁷²

5.71 In November 2017, the ATO noted that there was no enabling legislation or further public detail at that stage. This remained the status at May 2018.⁷³

Other reporting regimes

5.72 To address on-going cash activity and non-compliance in the building and construction sector a reporting regime was introduced in 2012 requiring certain businesses to report the total payments they make to each contractor for building and construction services each year.⁷⁴

5.73 The ATO website states that, to be compliant:

Businesses in the building and construction industry have to report to us the total amount they've paid you each year for building and construction services on the taxable payments annual report. This information allows us to identify those contractors who have:

- not included all their income on their tax return;
- not lodged tax returns or activity statements;

⁷² ATO, *Supplementary Submission 15.2*, p. 12.

⁷³ ATO, 'Phoenix-Taskforce-outcomes' < www.ato.gov.au/General/The-fight-against-tax-crime/Our-focus/Illegal-phoenix-activity/Phoenix-Taskforce-outcomes/ > viewed 8 May 2018.

⁷⁴ CAANZ, *Submission 3*, p. 5.

- not registered for GST where they are required to do so; and
- quoted the wrong ABN on their invoices.⁷⁵

5.74 There is no requirement for businesses to provide their contractors with details of the information reported but contractors may request the information.

5.75 Evidence to the Committee from Chartered Accountants Australia and New Zealand (CAANZ) suggested this reporting system may be deficient compared with a withholding at source tax regime to certain businesses sectors in New Zealand.⁷⁶ This is discussed in Chapter 6.

From cash to card

5.76 Significant and rapid changes affecting the global business environment over the last few years have also led to a reduction in the opportunity to commit cash-associated tax crime. For example, 'tap-and-go' payments,⁷⁷ as discussed below, have increased significantly. The primary change, over and above the acceleration of on-line transactions and the digitisation of government information, communication and services, has been the expansion and rapid adoption of cashless transactions for small and large sums.

5.77 While monetary policy is not within the jurisdiction of the ATO, the cash economy and responses to the cash economy may be influenced by the shift away from cash transactions. The Government, by enabling a technology that enables this shift, could be seen to be having an impact on those businesses which are operating legally, but under-report some cash income.

⁷⁵ ATO, *Contractors in the Building and Construction Industry*, updated 30 March 2017

<www.ato.gov.au/Business/Reports-and-returns/Taxable-payments-annual-report/Businesses-in-building-and-construction/Contractors-in-the-building-and-construction-industry/> viewed 13 March 2018.

⁷⁶ Mr Peter Vial, New Zealand Country Head and Tax Leader, Chartered Accountants Australia and New Zealand (CAANZ), *Committee Hansard*, Melbourne, 17 July 2017, p. 3.

⁷⁷ 'Tap and Go' payments do not require the use of a Personal Identification Number (PIN) at point of sale (for payments under \$100) and operate by microchip technology automatically transferring transaction information from consumer to vendor with a physical wave of a plastic debit or credit card over a payment terminal.

The potential of the cashless economy

5.78 As indicated above, there is acceleration away from cash transactions; even for low-value transactions with the use of contactless tap-and-go payment cards an increasingly popular form of payment. This reflects the widespread adoption of contactless functionality by merchants and consumer readiness to utilise such technologies. Indeed, a recent RBA survey reported that 85 per cent of survey respondents now hold a contactless card, compared to two-thirds back in 2013.⁷⁸ It is notable, however, that the Black Economy Taskforce has concluded that the risks of fraud through increasing tap-and-go limits outweighed any benefit for the consumer transaction experience.⁷⁹

5.79 Mr Richard Highfield, a former Tax Commissioner and tax expert, suggested:

I think there are already clear signs in Australia that we are moving towards a non-cash society. There is regular monitoring of the value of transactions that are effected electronically to make sales and purchases, and that clearly shows upward trends. Equally there is some fairly significant growth in numbers of particular denomination notes like the \$100 note and I think the \$50 note, et cetera. But I think in an aggregate sense you are seeing more and more transactions effected electronically. That includes business-to-business transactions and it also includes consumer-to-business transactions. I think these things are inevitable as technology becomes more ubiquitous.⁸⁰

5.80 Mr Timothy Reed, Chief Executive Officer, MYOB Australia, considered the shift to electronic transactions and the cashless economy would be more efficient and reduce the costs of doing business:

I believe that Australia would be well served by moving away from cash. That is only going to happen through regulation. I believe the cost of running a small business across the board would be lower if we moved to a cashless economy. The transactions that are captured electronically can flow in to this ecosystem that we are talking about. They can be captured by accounting

⁷⁸ See RBA, 'How Australians Pay: Evidence from the 2016 Consumer Payments Survey', *Research Discussion Paper, RDP 2017-04*, cited by Mr Simon Edwards, PayPal, *Committee Hansard*, Canberra, 16 August 2017, p. 2.

⁷⁹ *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 68.

⁸⁰ Mr Richard Highfield, Private capacity, *Committee Hansard*, Canberra, 14 June 2018, p. 3.

platforms such as the MYOB platform and can flow right through to the tax system.⁸¹

- 5.81 However, the Committee also heard from representatives of the Master Grocers Australia that, although its members are adopting standard business tools (ie Xero and MYOB) and the transition from cash to card for vendors is well advanced, this is not without stresses for small business.⁸² CEO Mr De Bruin maintained that the shift from cash disproportionately disadvantages small businesses compared with large:

We have no choice. It is a service. It is something the customer expects. We cannot reflect any costs back into margin, because margins are razor thin. Coles and Woolworths are what we call acquirers. They are banks in their own right. Their transaction costs are far less than ours. Our acquirers are the banks. We just absorb it.⁸³

Point-of-sale technologies and apps

- 5.82 While Australia is at the forefront of electronic card payments and contactless card use, some jurisdictions are more advanced in implementing fintech developments which support the shift away from cash.
- 5.83 As well as the proliferation of mobile payment apps, which are evolving more slowly in Australia, a number of other countries have progressed technologies which both register sales and convey transaction information directly to the revenue agency. These include early adopters like Sweden, and more recent developments in Russia and Italy.⁸⁴
- 5.84 At hearings, the ATO made it clear that facilitation of point-of-sale monitoring and the gathering of real-time tax information is not a priority. However, it is making progress in other areas, in particular through facilitation of real-time lodgement products and services for individuals and business. Mr Prouse of Xero Australia approved this approach, saying that

⁸¹Mr Timothy Reed, Chief Executive Officer, MYOB Australia Pty Ltd, *Committee Hansard*, Canberra 27 October 2017, p. 11.

⁸²Mr de Bruin, Chief Executive Officer, Ms Carmel Goldsmith, Member, Master Grocers Australia, *Committee Hansard*, Canberra, 25 October 2017, p. 8.

⁸³Mr de Bruin, Chief Executive Officer, Ms Carmel Goldsmith, Member, Master Grocers Australia, *Committee Hansard*, Canberra, 25 October 2017, p. 8.

⁸⁴See discussion Chapter 2, and Box 4.4 Use of Certified Cash Registers, OECD, *Tax Administration 2017*, p. 60.

real-time reportage is not a priority for small business either; they favour efficiency in the products being delivered by the ATO:

I think there is an advantage for the tax office, particularly if it comes with real-time payments [but]... The reality is that real-time reporting for small business is more about timely reporting and making that reporting simple. So we have had initiatives from the government for things like implementing a simpler BAS, which removes three fields from the business activity statement. But the business activity statement is still a two-page form.⁸⁵

- 5.85 Airwallex's Mr Joe McGuire, a former state manager for transaction banking with the Commonwealth Bank, however, proposed an innovative solution should government contemplate promoting a point-of-sale system, as have nations overseas:

The other opportunity that I would point out and which I think is a really exciting one for government is I have a bit of an idea of how you could dramatically increase your taxable revenue. Is everyone in the room aware of what a point-of-sales system would be for a merchant? I think there is a huge opportunity for government to build an API that all point of sales are mandated to plug into—to provide an API and attach with it a corporate card, which goes out to every customer. What this would do is: per transaction at a cafe, the 10 per cent GST would be paid out immediately to the government via the corporate card per transaction.⁸⁶

- 5.86 Mr McGuire elaborated the model, noting that the combination of the point-of-sale system and the issuing of the card would allow for both recording of cash transactions and modulating any cash liquidity issues that may result from immediate tax reconciliation:

...One of the biggest problems for collecting money at the moment for cafes is they take all of the cash transactions off the point-of-sale system and only pay tax on the credit cards. I think the other biggest challenge that you have for time-poor businesses is the BAS statements that come out every quarter as well. A way that you could do away with BAS statements and ensure that you collect all of the money is by—

...the ATO [issuing] to every business a card which is interest-free for 90 days and needs to be paid in full at the end of 90 days. So that is plugged in via API

⁸⁵ Mr Matthew Prouse, Partner Solutions Manager, Xero Australia Pty Ltd, *Committee Hansard*, Canberra, 27 October 2017, p. 3.

⁸⁶ Mr Joe McGuire, Global Head of Sales and Partnerships, Airwallex, *Committee Hansard*, Melbourne, 18 July 2017, p. 16.

to every point-of-sale system in Australia. For every transaction that goes through, the money is sent to the ATO. The ATO has a record of every financial transaction, so there is no requirement for a BAS statement. And just like a business does today, they just pay off their ATO or GST bill at the end of every 90 days.⁸⁷

Payment platforms, blockchain and identity verification

- 5.87 In the course of the inquiry, the Committee explored the potential of digital payment platforms and products to both introduce and reduce the risks of illicit activity, including tax crime associated with money laundering.
- 5.88 Evidence suggested that digital transfers and electronic platforms offer, overall, greater security for regulators than otherwise, however it is very important that regulatory frameworks and standards are consistent and robust, and information channels are free between partners. Both Airwallex and PayPal strongly emphasised this need for partnerships and information sharing between governments, third party businesses and agencies to support integrity in the burgeoning industry.
- 5.89 PayPal, for example, is the largest reporter to AUSTRAC of International Funds Transfer Instructions (IFTIs) in Australia, and works very closely with AUSTRAC as part of the Fintel Alliance.⁸⁸ However, PayPal's Director Mr Simon Edwards advised, that information sharing remains an issue:
- We have been encouraging AUSTRAC for some time to have a response loops. One of the problems for us is that for a long time we have been putting information into the system and not hearing anything back. That makes it difficult for us to improve our systems to know what to look for. Through the Fintel Alliance, AUSTRAC are now looking to try and provide that type of feedback loop. It's just part of our core business. If we facilitate activity that is illegal, we're not happy with it. It's very bad for our brand and very bad for our business. So we spend a lot of time and money trying to stop it.⁸⁹
- 5.90 As noted above the AML/CFT legislation aims to facilitate information sharing between agencies and the private sector. The Committee heard from the Digital Transformation Agency (DTA) about the importance of identity

⁸⁷Mr McGuire, Airwallex, *Committee Hansard*, Melbourne, 18 July 2017, p. 16.

⁸⁸ The Fintel Alliance, 'a world-first private-public partnership to combat money laundering and terrorism financing' was launched by AUSTRAC on 3 March 2017. See < austrac.gov.au/fintel-alliance-launch > viewed 19 April 2018.

⁸⁹ Mr Edwards, PayPal, *Committee Hansard*, Canberra, 16 August 2017, pp. 7–8.

verification in support of this approach, noting work being done by the RBA in this area.⁹⁰

- 5.91 The Attorney-General's Department also advised that it has been working closely with the ATO on a number of initiatives that fall under the National Identity Security Strategy; which include the implementation of the National Identity Proofing Guidelines (NIPGs) and using the Document Verification Service (DVS). These NIPGs provide a set of transparent recommended processes and requirements for identity verification for organisations which issue identity documents, and have been adopted by the ATO.⁹¹
- 5.92 Mr McGuire of Airwallex alerted the Committee to the further advantages of blockchain technology which is based on a disaggregated storage of information in multiple locations to ensure security of the client information shared, noting: 'Blockchain is, effectively, just a record held in multiple locations as opposed to at the RBA—a single source'.⁹²
- 5.93 Dr Chris Berg, of the RMIT Blockchain Innovation Hub, also advised of the utility of the technology for real time engagement with the ATO, to address the downstream effects on Australia's taxation system of the globalisation and networking of firms and of the gig economy. He recommended:

The ATO, in our view, should develop guidelines for real-time blockchain reporting that it would consider to be reasonably compliant. The ATO should also rethink its internal systems to facilitate voluntary real-time reporting. Real-time tax reporting raises different issues for individual taxpayers, however. Privacy is an overriding problem. There are new technologies that have been developed with the blockchain, such as zero knowledge proofs, that provide opportunities for privacy, protecting public services in the future.⁹³

The emergent risks of digital currencies

- 5.94 National governments are in the process of grappling with the policy and regulatory challenges associated with digital currencies as their use increases. In the context of money laundering and terrorism financing, the

⁹⁰ Mr Peter Alexander, Chief Digital Officer, Digital Transformation Agency (DTA), *Committee Hansard*, Canberra, 27 October 2018, p. 35.

⁹¹ AGD, *Submission 13*, p. 8.

⁹² Mr McGuire, Airwallex, *Committee Hansard*, Melbourne, 18 July 2017, pp. 15, 16.

⁹³ Dr Chris Berg, Private Capacity, *Committee Hansard*, Melbourne, 18 July 2017, p. 1.

Attorney-General's Department has summarised the key risks associated with digital currencies as:

- greater anonymity (or pseudonymity) compared with traditional non-cash payment methods;
- transactions are made on a peer-to-peer basis, generally outside the regulated financial systems; and
- different components of a digital currency system may be located in many countries and subject to varying degrees of AML/CTF oversight.⁹⁴

5.95 At hearings, the Department's Director, Financial Crime Section, Mr Daniel Mossop elaborated on these risks, and the challenges posed:

In terms of GDP it is a very small percentage, at the moment, but it is growing and the technology is quite new so it is evolving. Part of the problem with that is there is no intermediary point. It is as akin to cash as you can get and it is anonymous, by and large; it can be transferred peer to peer across great distances. Unlike cash you do not need to meet up to pass it over. It can travel to the other side of the country or the world almost instantaneously with no regulated industry in the middle. That is a particular challenge. You can start to imagine the sort of appeal it would have for people who are interested in criminal activity.⁹⁵

5.96 In addition, Airwallex's Ms Koh outlined some possible tax implications:

...it actually makes it a more pressing concern, purely because crypto currencies are relatively under-regulated and there are conceptual difficulties in trying to determine whether crypto currency is currency to begin with. So, for example, even the definition of crypto currency as money has attracted tax implications.⁹⁶

5.97 The Attorney-General's Department also highlighted the risk that cryptocurrencies could be used for money laundering of the proceeds of crime, however there are also protective factors:

⁹⁴ AGD, 'Regulating Digital Currencies under Australia's Anti Money Laundering/Counter Terrorism Financing Regime: Consultation paper', AGD, December 2016, p. 3. See further: AGD, *Report on the Statutory Review of the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 and Associated Rules and Regulations*, (AML/CTF Review), AGD, Canberra, April 2016, pp. 47–48; and in that report, FATF, 'Virtual Currencies: Key Definitions and Potential AML/CFT risks', pp. 9-12.

⁹⁵ Mr Daniel Mossop, Director, Financial Crime Section, AGD, *Committee Hansard*, 21 June 2017, p. 4.

⁹⁶ Ms Koh, Airwallex, *Committee Hansard*, Melbourne, 18 July 2017, pp. 15, 16.

There are a range of vulnerabilities around cryptocurrencies. They have this kind of pseudo-anonymity in peer-to-peer transfers, but there are also a range of factors that count against them in terms of being a good model for people to use to launder money on a large scale. Part of that is the volatility that they have. Moving money through digital currency means you can wipe off 50 per cent of the value overnight because the market moves, and, as I said earlier, as some stage you still have to cash in and cash out because, to be able to purchase goods in digital currencies, the market is still not enormous. It is, certainly, nowhere near akin to cash at the moment, so for most people they are still at a cash-in and cash-out point in being able to use that money. You lose a little bit of money at each end. You run the risk of the volatility in the middle.⁹⁷

- 5.98 Digital currencies will be discussed further under future challenges and solutions in Chapter 6.

Monetary measures and education

- 5.99 There was some discussion in the evidence about other measures to prompt a further shift away from cash use, including through illicit cash activity. In addition to the technology development discussed above, demonetisation and education approaches adopted overseas were reviewed.

Limiting cash circulation—demonetisation

- 5.100 Evidence provided that some countries have introduced cash regulatory measures to directly limit the use of cash for transactions, for example:

Capping the value of cash transactions was introduced in France with limit set at €1,000 from September 2016. This limit applies to transactions between consumers and businesses and business to business transactions but does not apply to transactions between individuals. It is of interest to note that the introduction of the limit was staged with the limit set at €3,000 prior to September 2016.⁹⁸

- 5.101 Other approaches to demonetisation of specific notes were briefly broached. It was noted, for example, that the Indian government in 2016 removed 500 and 1 000 rupee notes, requiring the old notes to be deposited

⁹⁷ Mr Daniel Mossop, Director, Financial Crime Section, AGD, *Committee Hansard*, Canberra, 21 June 2017, p. 8.

⁹⁸ Tax and Super Australia, *Submission 12*, p. 4.

or exchanged for new banknotes, with the stated aim of addressing counterfeit and black money activity.⁹⁹

5.102 Commissioner Jordan advised that there is a committee being formed to make recommendations to government on money control mechanisms, saying 'I think we have got to think a bit out of the box here. What are other countries doing that has been of use?'¹⁰⁰

5.103 However, the Tax Institute's Tax Counsel Ms Stephanie Caredes was cautious about cash control measures being introduced in Australia:

Looking at that point, it might cause some unnecessary or adverse impacts on people who are not actually participating in the black economy. So it might be unnecessary to require all wages to be paid electronically for everybody just because there are some people operating in the black economy.¹⁰¹

5.104 The Committee has noted the Black Economy Taskforce recommendation to outlaw cash payments in excess of \$10 000, above,¹⁰² and anticipates further outcomes of the committee of review, mentioned by the Tax Commissioner, and the research work recommended by the Taskforce to be undertaken by the RBA in the use and role of high denomination bank notes.¹⁰³

Education campaigns

5.105 Evidence referred to comparable jurisdictions in New Zealand and the United Kingdom that have introduced publicity campaigns to encourage people to report undeclared income:

- Her Majesty's Revenue and Customs (HMRC) has used a variety of publicity campaigns to encourage people to report undeclared income. HMRC also recently gained greater powers to obtain data from payment providers and business intermediaries to identify hidden economic activity.
- The New Zealand Inland Revenue (NZIR) is investing in a specific 'Hidden Economy' programme, complete with national marketing campaigns (e.g.

⁹⁹ Tax and Superannuation Australia, *Submission 12*, p. 4.

¹⁰⁰ Mr Jordan, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 9.

¹⁰¹ Ms Stephanie Caredes, Tax Counsel, The Tax Institute, *Committee Hansard*, Canberra, 6 September 2017, p. 6.

¹⁰² *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 51.

¹⁰³ *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 73.

‘Declare it all or risk everything’ and ‘Crackdown on Cashies’) targeting specific industries and raising awareness of the consequences of businesses avoiding tax obligations.

- The NZIR is also developing and enhancing relationships with local and national participants and stakeholders in specific industries on the importance of paying taxes, recording transactions, providing receipts and requesting invoices.¹⁰⁴

5.106 Commissioner Jordan has accepted that to support change in community attitudes to cash and compliance, a ‘significant education campaign’ is needed:

Into the future I can see a number of key strategies that we will need to, or will continue to, pursue and deliver on—very much a service ethic in the ATO, helping to facilitate people through what is a complex system; a focus on prevention rather than correction; greater and more sophisticated use of data for both service and compliance—it is important to use that for a service element as well; increased use of behavioural insights to help us work more constructively and collaboratively with taxpayers to get the right outcomes; increased digital offerings; leverage our relationships with industry; greater collaboration with the tax profession to tackle matters jointly; and to drive significant cultural change in the Australian community to perhaps the way some people approach their obligations, particularly around the cash economy and some of those issues where it might be okay to cheat a bit on our tax returns in our deductions. A significant education campaign is required there.¹⁰⁵

5.107 The Inspector-General of Taxation emphasised that both education campaigns and strong enforcement are required, especially for small business-based cash activity:

I do not think an education program on its own will work, but alongside strong enforcement action I think an education program can help. For example, we may move to a culture where, if a handyman comes and does some work for you and they say to you, ‘If you pay me cash it’s this much, but if you want a receipt it’s this much,’ you will always opt for the receipt. So I think we need to look at both of those... If they are not registered for anything at all and they take cash—an education campaign would be useful there. For example, if you do not have a receipt of any kind, or if you did not enter into a contract for certain work that is done, then you may not be able to sue if the

¹⁰⁴ Board of Taxation, *Submission 17*, Annexure A, and reproduced as Appendix D in this report.

¹⁰⁵ ATO, *Committee Hansard*, Canberra, 29 March 2017, pp. 1-2.

work is not done properly. An education campaign could point a lot of that out. The education campaign is, to a large degree, about education but it is also a little bit about deterrence by letting people know what the consequences are. That is why I am saying we need education and strong enforcement—you are letting people know that, if they do not do this, then that is going to happen.¹⁰⁶

- 5.108 An education campaign and promoting and reinforcing positive social norms around tax payment, including the role consumers play, was recommended by the Black Economy Taskforce, particularly in relation to migrant groups and visa holders.¹⁰⁷

Committee conclusion: what should Australia do?

- 5.109 The Australian Bureau of Statistics (ABS) has estimated that the non-observed economy (or cash and hidden economy) is approximately 1.5 per cent of Gross Domestic Product (GDP). This figure can be projected to be much lower than the real scale of activity— as indicated by the ATO's preliminary work in targeting this sector at the domestic level; the Black Economy Taskforce's 2018 estimation; and by extension, in collaboration with enforcement agencies and other nations to address serious tax evasion and profit shifting.¹⁰⁸
- 5.110 The ATO's submission has noted a 2010 World Bank study found Australia had the 11th smallest 'shadow economy' of 120 countries at the time.¹⁰⁹ While the problem may remain comparatively small in Australia, evidence would support the Australian National Audit Office (ANAO)'s view that the cash economy is 'a major tax integrity threat for the ATO, with a high risk rating'.¹¹⁰
- 5.111 The Committee continues to be concerned about the lack of data that exists on the exact size of the tax gap, including on reported and unreported income, and its sources. The Committee also remains sceptical that otherwise legitimate businesses represent a majority cause of the gap.

¹⁰⁶ Mr Ali Noroozi, Inspector-General of Taxation, *Committee Hansard*, Canberra, 10 May 2017, p. 4.

¹⁰⁷ *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 244.

¹⁰⁸ See ATO, *Submission 15*, p. 17.

¹⁰⁹ ATO, *Submission 15*, p. 17.

¹¹⁰ ANAO, 'Strategies and Activities to Address the Cash and Hidden Economy', *ANAO Report No.27 2015–16*, p. 26.

- 5.112 In particular, the Committee questions whether under reported income from coffee shops, beauty salons and hairdressers could be the equivalent of three per cent of GDP, as recently estimated by the ABS.¹¹¹ Rather the Committee considers it more likely that the majority is the result of illicit activity. Indeed, it is of greater concern that 18 years after this issue was first seen as serious, and now has possibly doubled, that its source remains a matter of debate.
- 5.113 Therefore, while the Committee accepts the ANAO's conclusion that the ATO's strategies to address the cash and hidden economy are on par with other nations and, moreover, are 'sound and increasingly cost effective', it urges the ATO to do more. Other countries provide pragmatic approaches which the Committee believes could immediately reduce the circulation of illegal cash funds in the domestic economy.

Cash

- 5.114 One option would be to require businesses trading in cash to use a certified cash register, as in Sweden. This could be an expensive policy option so, for example, if the register was to cost 1 700 Euros (approximately \$2 700¹¹²) and two million Australian businesses were required to purchase one, this would result in an upfront compliance cost of \$5.6 billion. Such a cost would be unlikely to pass a cost benefit test at present time.
- 5.115 Similarly, if Australia was to remove \$50 and \$100 notes in a similar way to the Indian demonetisation this may not be successful in reducing illegal cash activity as those individuals could simply move on to using other Australian notes or potentially the higher value notes of a foreign currency. Given the lack of available information in the Australian sphere the Black economy Taskforce has recommended the Reserve Bank of Australia study the use and prevalence of the higher denomination notes, in particular the \$100 note.¹¹³
- 5.116 The French system of limiting cash transactions may make it more difficult for some individuals to make large transactions; however, this would probably have no impact on the businesses that under-report cash income in

¹¹¹ Recent ABS estimates suggest the black economy as a proportion of GDP has doubled—to three percent, or approximately \$50 billion per year. Cited in *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 23.

¹¹² As at 22 March 2018 Euro conversion to Australian dollars.

¹¹³ *Black Economy Taskforce Final Report*, October 2017 (May 2018), p. 49.

small value transactions. The prohibition announced by Government on cash payments of greater than \$10 000 in the 2018–19 Federal Budget is a significantly larger cash threshold than that of France, and is thus more likely to impact money laundering activity or building industry payments.

Withholding tax changes

- 5.117 Mr Vial of CAANZ, among some other witnesses, argued for the utility of revising existing policies to mirror reforms in New Zealand in regard to PAYG withholding in relation to high risk industries, such as the Australian building and construction industry.¹¹⁴
- 5.118 Following New Zealand’s example, this could be extended to other ‘at risk’ industries, with an assessment of whether the additional compliance costs on the industries would be outweighed by the increased revenue. The Committee did not receive specific evidence on the effectiveness of the reporting regime for the building and construction industry, although this was highlighted in ATO publications.
- 5.119 The Taskforce highlighted the success of the contractor payment reporting scheme operating in Australia (the TPRS) which covers select high-risk industries, initially in the building and construction sector, extended in the 2017–18 Budget to couriers and cleaning services and due to be extended to security providers, road freight transport and IT contractors.
- 5.120 Further discussion on this is in Chapter 6, following consideration of the implications of the gig and sharing economies. The Committee considers that such a change be considered by the Treasury, taking into account the effectiveness of the current policy.

Social contract policies

- 5.121 One inquiry participant suggested a tax and social contract response and so that those operating in the black economy ‘should not enjoy all the entitlements and protections afforded to law abiding members of the community, such as:
- to deny landlords standing at law unless they have tax compliance certification;
 - deny consumer protections to complainants without a valid tax invoice from business in dispute;

¹¹⁴ Mr Vial, CAANZ, *Committee Hansard*, Melbourne 17 July 2017, p. 5.

- business licensing and renewal conditional on possession of tax compliance certificate;
- contractor compensation and public liability claims would require presentation of a valid tax invoice issued by the injured service provider.¹¹⁵

5.122 The Committee is cautious in supporting these approaches which on face value could encourage compliance with tax laws, given, they may act as an incentive for a certain proportion of individuals to move completely out of the formal system or result in cost shifting to other government organisations, such as an injured service provider denied coverage, seeking medical assistance at a public hospital.

Black Economy Taskforce findings

5.123 This chapter has investigated how under-declaration of funds by some businesses can destabilise those firms who are honouring their obligations to the ATO and other regulators.

5.124 Discussion addressed the potential for fraudulent registration under the Australian Business Number (ABN) system and deficiencies in corporate registration managed by the Australian Securities and Investments Commission (ASIC), and how this facilitates illegal phoenix activity.

5.125 The nexus between tax avoidance and criminal activity was another area of concern, with activities in the retail tobacco sector highlighting a lack of effective regulation and appropriate enforcement powers at local level, an entry point to effect prosecution for these illegal activities. Meanwhile, the potential to contain global money laundering activities was discussed in the context of the evolving international payment market along with the emergence of digital currencies.

5.126 During the course of this inquiry, amendments to Australia's Anti-Money Laundering and Counter-Terrorism Financing (AML/CTF) framework were passed with the specific intention to improve security and compliance in the evolving digital payment and currency markets. The amended legislation aims to improve information sharing between government regulators and agencies, such as the ATO and ASIC, as well as third party (private) fintech participants.

5.127 The release of the final report of the Government's Black Economy Taskforce was anticipated by the ATO to be influential on its policy and program

¹¹⁵ CAANZ, *Submission 3*, p. 4.

settings to address problems associated with the cash economy, and within the broader framework of measures needed that are beyond the jurisdiction of taxation.¹¹⁶

5.128 The publication of the Taskforce's final report coincided with the release of the 2018–19 Federal Budget on 8 May 2018.¹¹⁷ In the Budget, the Government allocated funds for a number of new measures in response to the final report, including:

- increasing the ability of enforcement agencies to detect and disrupt black economy participants.
- removing the unfair advantage black economy participation gives businesses by removing deductions for non-compliant payments and changing the Government's procurement procedures to incentivise tax compliance in supply chains.
- consulting on reforms to the Australian Business Number (ABN) system to improve the confidence the community has in identifying who they are dealing with, including development of rigorous new identification systems for company directors (DINs).
- introducing an economy-wide cash payment limit for large cash transactions of \$10 000 to reduce the ability of black economy operators to use cash to avoid their tax and reporting obligations and launder the proceeds of crime.
- providing additional funding to the Tax Practitioners Board to take action against tax agents that facilitate activity in the black economy.
- expanding the taxable payments reporting system to contractors in industries with higher identified risks of not reporting their income.¹¹⁸

5.129 The Government also announced funding for an Illicit Tobacco Taskforce to disrupt organised crime groups operating in illicit tobacco importation and

¹¹⁶ ATO, *Submission 2, Inquiry into the 2016–17 Annual Report of the ATO*, p. 13.

¹¹⁷ The Hon Kelly O'Dwyer, Minister for Revenue and Financial Services, 'Tackling Illegal Behaviour in the Black Economy', *Media Release*, 8 May 2018 <kmo.ministers.treasury.gov.au/media-release/051-2018/> and see the *Black Economy Taskforce Final Report*, October 2017, <static.treasury.gov.au/uploads/sites/1/2018/05/Black-Economy-Taskforce_Final-Report.pdf> viewed 9 May 2018.

¹¹⁸ *Budget 2018–19, 'Protecting the Integrity of the Tax System'*, Overview <www.budget.gov.au/2018-19/content/overview.html> viewed 9 May 2018.

retail, with the taxing point of tobacco to be made at entry into Australia to choke the illegal tobacco market.¹¹⁹

5.130 These measures satisfy a number of proposals made to address concerns around cash activity raised in this chapter. Some also have bearing on recommendations made for the broader reform of the taxation system to improve its integrity and support taxpayer confidence, as discussed in the final chapter of this report.

¹¹⁹ *Budget 2018–19, Overview*, viewed 9 May 2018.

6. Challenges and solutions

Introduction

6.1 The tax system has been described as an eco-system—with interdependent players at all levels having an impact on how well the system operates. As such, there are a number of key influencers of taxpayer behaviour and the way they engage with the tax system including:

- ease and costs of compliance;
- sense of procedural justice and fairness in how the system works;
- perceptions of other taxpayers' compliance and how non-compliance is dealt with;
- trust and confidence in the Australian Taxation Office (ATO);
- social norms;
- personal beliefs such as fulfilling a sense of duty;
- risk appetite and the desire to avoid being caught or being penalised; and
- financial pressure and economic conditions.¹

6.2 This chapter identifies the primary challenges Australia's tax system faces in the near to medium term and some key challenges for the ATO in maintaining, and improving on, the existing high levels of taxpayer engagement.

¹ 'Commissioner's Forward', ATO, *Submission 20*, pp. 3–4.

- 6.3 The chapter discusses the impact of changes in workforce arrangements on the tax system and the issue of work-related expense deductions. It also addresses the risks of leaving people behind in the digital future, along with maintaining security of the tax system and taxpayer privacy in the evolving digital realm.
- 6.4 Finally, the chapter concludes the report in examining the latest system developments affecting the economy—the Financial Technology (fintech) sector and digital currencies—and the potential threats these pose to the stability of the tax system and taxpayer engagement more broadly.

Changes to the workforce

- 6.5 The Committee has heard, during its inquiry, about the changes in the workforce resulting from the trend to contract employment, rather than ‘traditional’ employer–employee relationships.
- 6.6 The rise of the contractor and of corporate sole traders, with more corporate structures and favourable deductions, could lead to Pay As You Go (PAYG) stream implications for tax collection. The problem is that the ATO will obtain fewer regular tax receipts and less surety of tax collection. From a superannuation perspective, some people are being classified by employers as contractors instead of as employees—and so these people may be missing out on their eligibility for superannuation guarantee contributions and regular PAYG withholding tax payments, thus creating disengagement from the tax and super system.
- 6.7 The Institute of Public Accountants (IPA) observed that:

...the growing number of self-employed businesses acting as contractors poses to the ATO a greater risk of losing tax revenue when compared to collecting PAYG from employed individuals’. Contracting has increased to 10 per cent of the workforce - driven by the sharing economy through online IT and mobiles, and incentives under the tax system, including greater employment deductibility, lower taxes and potential for income splitting.²

The gig economy and the sharing economy

- 6.8 One of the reasons for the increase in this type of worker category is the rapid proliferation of two relatively new concepts—people working in the

²The Institute of Public Accountants (IPA), *Submission 2*, p. 3.

‘gig economy’ and those operating in the ‘sharing economy’. Much of this transformation of the labour force developed over the last ten years with considerable restructure in Australian workplaces through offshoring of functions, online retail, greater automation and self-service in the economy and more portable, cheaper and connected tools of trade. Added to that was structural change following the resources boom. A considerable amount of labour moved from a full-time single employer model to a multi-job flexible and ‘uncertain hours’ model. Many of these jobs were self-created ‘gigs’ through freelance work or contracting.³ A wide variety of workers now fall into this category.

6.9 The gig economy tends to create cheaper labour in competition with traditional arrangements and as a consequence gig workers/contractors are a competitive labour hire option and thus a growing section of the labour market. However, this distinction may be exploited when, say, people who almost exclusively work together as a team with essentially the same functions and business goal are classified differently as contractor or employee in each other’s business.

6.10 The ATO provides a six part guide to the definition of a contractor versus an employee on its website. The basic difference given is that an employee works in your business *as a part of your business* while a contractor is running *their own business*. As the ATO states—

It’s against the law for a business to incorrectly treat their employees as contractors. Businesses that do this are:

- not meeting their tax and super obligations;
- denying workers their employee entitlements; and
- illegally reducing their labour costs and gaining an unfair advantage over their competitors.⁴

6.11 The ATO’s web information on this matter, which includes a video on common myths, indicates that this distinction is difficult to determine and enforce. Further details of employer tax engagement obligations, depending on classification, are as follows:

If your worker is an employee you’ll need to:

³ The Australian Government the Treasury, *Black Economy Taskforce Interim Report*, March 2017, p. 138.

⁴ ATO, Difference between Employees and Contractors <www.ato.gov.au/Business/Employee-or-contractor/Difference-between-employees-and-contractors/> viewed 12 March 2018.

- withhold tax (PAYG withholding) from their wages and report and pay the withheld amounts to us;
- pay super, at least quarterly, for eligible employees;
- report and pay fringe benefits tax (FBT) if you provide your employee with fringe benefits.

If your worker is a contractor:

- they generally look after their own tax obligations, so you don't have to withhold from payments to them unless they don't quote their ABN [Australian Business Number] to you, or you have a voluntary agreement with them to withhold tax from their payments;
- you may still have to pay super for individual contractors if the contract is principally for their labour;
- you don't have FBT obligations.⁵

6.12 The difficulty in determining this distinction was previously discussed in more detail in Chapter 3.

6.13 The Institute of Public Accountants (IPA) considered the more generous tax treatment of a contractor operating under a corporate structure, means:

The tax system also incentivises individuals to contracting due to the perceived tax advantages. The tax advantages include the ability to claim a greater range of deductions than an employee, access to lower tax rates and income splitting opportunities. The lower income rate for incorporated businesses has further exacerbated the incentives for a contractor to use a corporate structure to gain access to more favourable tax rates. Employers too are attracted to using contractors as a way to reduce employee on-cost such as superannuation guarantee, leave entitlements and payroll tax.⁶

6.14 From a specific tax perspective, one issue is that tax returns for contractors are not required until after the end of the next year, and longer—up to 22 months—if using tax agents, with the delays impacting the Government's revenue. It can also result in tax compliance issues as the contractors must prepare and have available the necessary funds to meet their delayed tax obligations. As the IPA stated, for the starting-out contractor:

⁵ See ATO, Your Tax and Super Obligations < www.ato.gov.au/Business/Employee-or-contractor/Your-tax-and-super-obligations/ > viewed 12 March 2018.

⁶ IPA, *Submission 2*, p. 3.

This can impose a burden—first year tax and then some of second year PAYG instalments for which they may have not budgeted.⁷

- 6.15 The ‘sharing economy’ or ‘collaborative economy’ is often part of the gig economy. It has been described as a ‘peer-to-peer’ (P2P) based activity—acquiring, providing or sharing access to goods and services; and facilitated by a community-based on-line platform.⁸ The concept is based on the assumption that under-used private assets can be utilised for a market value and, as such, are cheaper than established markets. This economy has now expanded to encompass offerings like on-line share platforms advertising open work spaces for freelancers in the gig economy. The current forecasts are that this market will increase in value some 20 fold over the next ten years. A well-known example of the sharing economy which utilises people in the gig economy is Uber (a share ride system operating with private vehicles, akin to an unlicensed taxi market).
- 6.16 The sharing economy continues to face regulatory and tax evasion contentions for the sharing platforms per se, which take a commission from users. But it is the rise of the gig economy, and its potential disengagement from the tax and superannuation systems, which will require the most monitoring and enforcement over the foreseeable future. This was explored by the Black Economy Taskforce, recommending that operators of designated sharing economy websites should be required to report payments made to their users to the ATO; and also proposing initiatives to counter ‘sham contracting’ (contractors who have a contrived business-to-business relationship).⁹
- 6.17 Chapter 3 discussed Personal Services Income (PSI) rules in relation to contractor based employment with big sharing companies.

Withholding tax

- 6.18 As discussed in the preceding section, the number of contractors as a proportion of workers is rising. The primary issue related to workers operating as contractors from a tax perspective is that under current arrangements ABN holders are excluded from the PAYG withholding tax

⁷ IPA, *Submission 2*, p. 3.

⁸ Definition at <www.investopedia.com/terms/s/sharing-economy.asp> viewed 12 March 2018.

⁹ The Australian Government the Treasury, *Black Economy Taskforce Interim Report*, March 2017, p. 231.

system which provides for the regular payment of tax and superannuation obligations.

- 6.19 To combat the uncertainty and preserve timeliness in tax-related payments associated with contract work, the New Zealand tax system has introduced a contractor withholding tax at source system for self-employed businesses.
- 6.20 New Zealand's comprehensive withholding tax regime does not require reporting by sectors at risk of non-compliance, as was recently advanced by the ATO. New Zealand has instead legislated to impose withholding tax at various rates on a whole range of identified at risk occupations, vocations or activities. The regime has recently been widened.¹⁰
- 6.21 Mr Peter Vial, New Zealand Country Head and Tax Leader for the Chartered Accountants of Australia and New Zealand (CAANZ), highlighted the role of New Zealand's Generic Taxation Policy Process (GTPP) in securing these reforms. According to Mr Vial, the GTPP is 'the jewel in [NZ's] tax policy crown', and has been 'instrumental in ensuring our legislation and policy is more cohesive, more robust and fair and efficient than it might otherwise have been'.¹¹
- 6.22 The GTPP is an 'end to end process', which guides how the taxpayer, and the business community in particular, engage with the tax system and 'how they input into tax policy and law as it's developed':

It starts off with the government setting its tax policy work program, which is usually for an 18-month period. The government consults with stakeholders like us and other key private sector stakeholders on what reforms should be on that program and what we would like included, and we often get measures or issues included on that work program. Then officials consult with the community, and particularly with the key stakeholders, as they develop the policy and turn it into law. By the time the legislative stage is reached and a bill is introduced, many, but often not all, of the issues and risks and drafting challenges have already been addressed. If not addressed, they have at least been aired and they are on the table.¹²

- 6.23 Mr Vial said that the New Zealand withholding regime, which has been in place for several decades, has captured and kept contractors in the tax

¹⁰ Mr Peter Vial, New Zealand Country Head and Tax Leader, Chartered Accountants of Australia and New Zealand (CAANZ), *Committee Hansard*, Melbourne, 17 July 2017, p. 3.

¹¹ Mr Vial, CAANZ, *Committee Hansard*, Melbourne 17 July 2017, p. 3

¹² Mr Vial, CAANZ, *Committee Hansard*, Melbourne 17 July 2017, p. 3.

system. Recent amendments to the schedules had further expanded scope while allowing flexibility to the taxpayer:

For example, if you're a journalist working as a stringer writing articles, or you are in a particular industry where your work is on contract and ad hoc, you are likely to be included as a vocation or activity in the schedule, subject to a withholding tax rate. The new changes allow people who are even outside that particular scheduler approach to elect into the withholding payment regime and to have tax deducted at source. It also allows them to elect their own rate of withholding tax, subject to minimums. So the regime has been broadened and made more flexible, and it has also been given some more teeth.¹³

Recommendation 6

6.24 Based on the New Zealand system, the Committee recommends that Treasury considers an ABN withholding tax system at source for all industries with the potential for the rates to be industry specific.

6.25 As the New Zealand system demonstrates, this could be a defensible system, particularly for industries that engage in extensive contracting. Within Australia experience from the mandatory reporting requirements introduced for the construction industry has suggested that such interventions have potential to reverse 'entrenched longstanding non-compliance'.¹⁴

6.26 In addition, the Committee is of the view that the contractor assessment tool provided by the ATO could be improved, with reference to the tool developed by the Her Majesty's Revenue and Customs (HRMC UK) which has more in-depth and well targeted questions, to reduce errors and uncertainty.¹⁵

Recommendation 7

6.27 The Committee recommends the ATO should review the functionality of the contractor assessment tool for accuracy and utility to taxpayers by reference to the functionality of the tool deployed in the United Kingdom, and report to the Committee on its progress.

¹³ Mr Vial, CAANZ, *Committee Hansard*, Melbourne 17 July 2017, p. 3.

¹⁴ IPA, *Submission 2*, p. 5.

¹⁵ For a question by question comparative assessment see Tax and Super Australia, *Submission 12.1*, pp. 1–5.

Workplace deductions

6.28 During the conduct of the inquiry it was evident that the treatment of workplace deductions will need to be considered in the future. The issue of deductions was raised in relation to the possibility of eliminating the need for individuals to lodge tax returns. While the income elements of the tax return can now be pre-filled (effectively automated) it is primarily the inclusion of workplace deductions that would prevent the elimination of tax returns for most individuals.¹⁶

6.29 In New Zealand taxpayers do not need to lodge a tax return. Mr Vial, CAANZ's New Zealand Country Head and Tax Leader, explained how this was achieved:

...many New Zealanders do not, and are not required to, file income tax returns. Most individual taxpayers are unable to claim work-related deductions. Generally taxpayers who derive only wage and salary income and interest from dividends do not file tax returns. The reason they do not file tax returns is that their tax has been deducted at source and they're not entitled to claim deductions other than in very narrow circumstances.¹⁷

6.30 He further explained that one of the two allowable deductions is for the preparation of a tax return,¹⁸ which wouldn't be required if you have not incurred premiums for loss of income insurance, the only other allowable deduction:

We have only two types of work related deduction that a wage or salary earner could claim. One is in relation to income protection insurance premiums, and many or most of them don't have such insurance. The other is for the cost of preparing a return. Given that most of them don't have to file returns, they are not entitled to a deduction for something they're not incurring.¹⁹

6.31 Other countries have a similar approach to New Zealand, including the UK. In Denmark, Sweden and Norway tax returns are completely pre-filled, requiring a positive response as acceptance in Sweden and a silent response in Denmark and Norway. This 'push return' approach is possible because

¹⁶ Mr Highfield, Private Capacity, *Committee Hansard*, Canberra, 14 June 2017, pp. 6–7.

¹⁷ Mr Vial, CAANZ, *Committee Hansard*, 17 July 2017, p. 2.

¹⁸ A much narrower definition than 'costs of managing tax affairs' which applies in Australia.

¹⁹ Mr Vial, CAANZ, *Committee Hansard*, 17 July 2017, p. 2.

their systems 'feature comprehensive withholding mechanisms and little or no deductibility for expenses'.²⁰ Note, however, as discussed in Chapter 2, the Inspector-General of Taxation cautioned the comparison against other tax systems where there may have been minimal ability to claim deductions before pre-filing anyway, and noting the 'different socio-economic and legal frameworks in each system', and as such, different cultural expectations and impediments.²¹

6.32 Some participants have argued that Australia's current treatment of workplace deductions is unique (and negatively so) amongst other OECD countries. The Tax Institute argued that:

Other countries provide only very limited and narrow circumstances where work-related expenses can be claimed.²²

6.33 The Institute's submission also urged:

Implement Henry Tax review [*Australia's Future Taxation System*, AFTS review] Recommendation 11: Australia introduce a standard Workplace Expenses deduction, while retaining ability to claim more with full substantiation above threshold.²³

6.34 Mr Richard Highfield provided a table based on information included in the OECD's 2006 tax review, which showed the various treatments of work place deductions in comparable countries. Australia and Denmark's schemes were rated as more generous than other nations.²⁴ The Tax Institute noted that in other OECD countries where final withholding and no deductibility for work-related expenditure feature, most people do not have to lodge a return.²⁵

²⁰ IGT, *Submission 5*, p. 24.

²¹ Inspector –General of Taxation, *Submission 5*, p. 26.

²² The Tax Institute, *Submission 16*, p. 5.

²³ The Tax Institute, *Submission 16*, p. 7, citing recommendations in the Australia's Future Tax System Final Report. Referred to as the Henry Review, see *Australia's Future Taxation System (AFTS) Report to the Treasurer*, December 2009, released May 2010 <taxreview.treasury.gov.au/content/Content.aspx?doc=html/pubs_reports.htm> viewed 12 March 2018

²⁴ Rated from not available (New Zealand, Spain) to narrow (Ireland, Netherlands, Switzerland, United Kingdom) to limited (Canada, Japan, United States). See Annex 2 in Mr Richard Highfield, *Submission 6*, p. 25.

²⁵ The Tax Institute, *Submission 16*, p. 5.

6.35 Mr Highfield elaborated on other nations' workplace deductions requirements during a public hearing:

As I mentioned, there are countries where certainly the rules for deductibility are much tighter. For example, it has to be a condition of your employment. There has to be an authorisation by your employer that a car was required to be used for this particular purpose over this period of time or whatever. So there are much more extensive tests undertaken to validate deduction claims.²⁶

6.36 He questioned the nexus between valid work-related motor vehicle travel and work-related travel claims which are being claimed by three in 10 workers in Australia:

As it happens, motor vehicle expenses are the most common work-related expense deduction. Over 30 per cent of employees are claiming a deduction for work-related expenses. When you bear in mind that travel to and from work is not deductible, it is very hard to rationalise how almost one in three employees can justify use of their car for their work. Certainly there are occupations where it is valid and acceptable, but one in three?²⁷

6.37 The different treatments of workplace expense deductions emerged as a focus in discussion of tax simplification during the inquiry. Mr Highfield argued that: 'Reform of WREs is long overdue given the compliance burden they create and the likely revenue leakage involved'.²⁸ He quoted the AFTS Henry tax review, findings that:

There is a high degree of variation in WRE claims among individuals with identical occupations and income levels. This variability could be explained by: some taxpayers over-claiming (including expenses that might be private, domestic or capital in nature), given the limited ability of the ATO to audit WREs; some taxpayers interpreting expenses that are incurred in performing their job differently from other taxpayers (raising issues of complexity and transparency in the system); and differences in employer behaviour, where some employers pay for a particular type of expense while other employers do not.

In Canada, a country with a similar tax system and administrative arrangements to Australia, it is estimated that 10 to 15 per cent of WRE claims each year are invalid. If over-claims in Australia are of a similar order, this

²⁶ Mr Highfield *Committee Hansard*, Canberra 14 June 2017, pp. 6–7.

²⁷ Mr Highfield, Private capacity, *Committee Hansard*, Canberra 14 June 2017, pp. 6–7.

²⁸ Mr Richard Highfield, *Submission 6*, p. 11.

would equate to an over-claim of between \$1.4 and \$2.1 billion in 2006–07. While no tax system can achieve perfect compliance, the potential magnitude of non-compliance suggests that administrative solutions alone cannot address this issue.²⁹

- 6.38 CAANZ's Mr Vial considered that an overhaul of Australia's workplace deduction system would probably need to be part of a more systematic review to make it palatable to individual taxpayers accustomed to the claims system:

My view is that the removal of the entitlement was achieved with little fuss because the change was made as part of a package of reforms that included within a very short space of time reductions in tax rates, the introduction of our very comprehensive GST, and increases in social assistance. The packaging of tax reforms has been successful on a number of occasions in New Zealand, and that's just one of them.³⁰

- 6.39 The Tax Institute also suggested that Australia should refer to New Zealand, and to the United Kingdom model, to achieve more streamlined processes for individuals with simple tax affairs.³¹

- 6.40 CPA Australia agreed that, while not actually favouring change, any review of the current work-related expense deduction system should be part of a wider review. Mr Paul Drum, Head of Policy, CPA Australia stated:

One of the things that I did want to raise is that quite often in inquiries such as this, Chair, where issues of tax complexity are considered, the issue of either eliminating or capping allowable deductions for work-related expenses incurred in the derivation of one's income is often raised under the guise of simplifying the tax system.

In other inquiries, this is not something that we have supported on the basis of an exclusive simplification measure and certainly not as a budget repair measure either. It is something that we could entertain as part of a broader review of the tax system. But if it is cherry-picked, the items are picked out one by one, we are not supportive of that approach.³²

²⁹ Australian Government, AFTS Review, vol.1, Personal Tax, December 2009, p. 5, cited in Mr Richard Highfield, *Submission 6*, p. 11.

³⁰ Mr Vial, CAANZ, *Committee Hansard*, Melbourne 17 July 2017, p. 2.

³¹ The Tax Institute, *Submission 16*, p. 6.

³² Mr Paul Drum, Head of Policy, CPA Australia, *Committee Hansard*, Melbourne, 18 July 2017, p. 1.

- 6.41 He further elaborated on the Commissioner of Taxation's public statement on the disproportionately high number of Australian taxpayers claiming certain work-related expenses:

He talked in a recent speech, for example, to the National Press Club, where he said half of all Australians are claiming laundry expenses and how could that be. So that does raise a red flag in the system and it raises questions that need to be answered. There are questions about travel expenses that people are claiming. We note that given 74 per cent of returns are prepared by tax agents, some of these claims that are now under question will be prepared by tax agents. We ask: how can that be? How can they be so different to what we would expect?³³

Committee conclusion

- 6.42 The Committee views a reform of the treatment of individual taxpayer work-related tax deductions to be important. This initiative would be in step with countries that have adopted 'push returns' for the majority of individual taxpayers with uncomplicated tax affairs. Evidence to the inquiry indicates that the high level of tax agent use by taxpayers with very straightforward tax situations is partly associated with an expectation that an agent will advise of deduction claims.
- 6.43 In many cases, individual taxpayers employing an agent to prepare their return on their behalf will now have an almost completed tax return pre-filled by the tax administrator. Therefore, the ability of a taxpayer to choose a standard deduction, or to substantiate every claim above the determined threshold, will streamline tax return lodgement and reduce compliance costs for many taxpayers. It will also have the effect of tightening the nexus between income earned and substantiated claims as there will be fewer of these in the system.
- 6.44 Furthermore, it will also reduce the potential for unfairness in the system when people cheat or when their workplaces have differing practices (for instance, legitimate laundering expenses for those wearing a 'uniform').

³³ Mr Drum, CPA Australia, *Committee Hansard*, Melbourne, 18 July 2017, p. 1.

Recommendation 8

6.45 The Committee recommends that the work-related deductions scheme be reformed by introducing the standard deduction concept as proposed by the Australia’s Future Tax System Review.

Fairness would be maintained by enabling individuals to claim above the set amount by providing full substantiation through a tax return process.

6.46 This recommendation will align with the ATO’s plan to introduce a ‘push’ tax return (as discussed in Chapter 4).

The ATO and technology change

6.47 The ATO is responding to digital innovation which holds many benefits for Australia’s tax system, especially given Australia’s transfer payments are often dependent on information received by the ATO and that the ATO oversees other administered programs like the Private Health Insurance Rebate and First Home Saver Accounts Scheme. The benefits of digitised systems and high level computational capacity have been previously discussed in Chapters 2 and 3. However, these new systems and applications bring challenges in transition.

Is digital transition alienating some citizens?

6.48 While the digital revolution has brought many benefits to the tax, superannuation and transfer systems, it has also brought negatives. The most concerning from an economic stand-point—and not only at the citizen-level but also at the tax administration level and more broadly for the ongoing stability of commerce and the economy—is the rise in cyber-crime and scams. The Australian Competition and Consumer Commission (ACCC) has recorded a reported loss to Australian citizens from cyber-crime and identity scams of almost \$300 million in 2016.³⁴ This alone is enough

³⁴ ‘In 2016, the Australian Competition and Consumer Commission (ACCC) and the Australian Cybercrime Online Reporting Network (ACORN) received a combined 20 0103 reports about scams. Losses reported to Scamwatch, ACORN and from other scam disruption programs totalled almost \$300 million. This figure is by no means conclusive of the total cost of scams as many victims do not report their experiences—in fact in April 2016 the ABS published results of its Personal Fraud survey, which estimated the total amount lost to personal fraud to be closer to \$3 billion.’ Excerpt from: ACCC Report, *Targeting Scams—Report of the ACCC on Scams Activity 2016*, May 2017, Foreword, p. i < www.accc.gov.au/publications/targeting-scams-report-on-scam-activity/targeting-scams-report-of-the-accc-on-scam-activity-2016> viewed 25 May 2017.

reason to understand why non-digitally savvy citizens shy away from, or refuse to engage with, internet-based personal data, reporting or banking systems. The Committee did not receive direct feedback on this occurrence but the nature of digitised Committee advertising processes would tend to exclude a digitally averse group.

- 6.49 Some people are not engaging with the new digital interface—which is the first-line engagement interface of the ATO—because it is unfamiliar and they aren't ICT confident. These people are likely to become increasingly disengaged from knowledge of their own affairs and information about the system as a whole. Instead of a world of greater information, which digitisation is able to offer, theirs becomes progressively smaller.³⁵ This is particularly concerning as the growing proportion of older Australians will hold the majority of household wealth, not only in retirement savings but also in valuable principal residences.
- 6.50 The ATO's own website details the threats to an individual's wealth through identity theft, which includes, amongst others:
- Accessing your myGov account;
 - Stealing your superannuation;
 - Selling your house;
 - Creating fake businesses and committing refund fraud in your name; and
 - Selling your identity to organised crime groups on the dark web or via other means.³⁶
- 6.51 The ATO goes on to say that 'thieves need some basic details such as name, date of birth, address, myGov details or tax file number (TFN) to commit identity crime'. And it further warns digital non-natives that:

³⁵ For example, hard copy tax return lodgement instructions are no longer available in print at myGov Shopfronts. Citizens seeking the hard copy are generally unfamiliar with online presentation and/or have concerns about access (vision or fund limitations) or security (little to no personal ICT systems security) and many don't have mobile devices for web-reading. Taxpayers are advised, on the ATO website, that these publications are not available at the myGov sites and to call a number provided for assistance. However, to obtain a non-digital resource presumes the use of a digital system first—or face-to-face disappointment when the request at the myGov Shopfront is declined.

³⁶ ATO Cyber-crime Warnings online < www.ato.gov.au/General/Online-services/Identity-security/Protecting-your-information/> viewed 13 March 2018.

If criminals steal your identity, it can take a long time to fix. It may be difficult for you to get a job, a loan, rent a house, or apply for government services or benefits.³⁷

6.52 The ACCC identified in its last Scam Report a number of relevant issues for the digital inclusion of particular groups in the tax system, finding that:

- The 65 and over age group was statistically more likely to send money when encountering fraud; and
- Older groups were also more likely to fall victim to computer support fraud (remote access scams), due to their lower level of knowledge and confidence in using modern technologies.

6.53 A casual observer would infer that a taxpayer placing their information in a new digital set-up, with little expertise in the subject matter or the tools of application, bears much risk and few rewards. It is therefore unsurprising to note the uptake of tax professionals lodging individual tax returns in Australia. The cautious will offset their risk by engaging an agent. For those who have been self-lodgers but have experienced a malicious attack or 'near miss' in the absence of accessible non-digital resources, they may choose to risk the consequences of disengagement.

6.54 The Tax Commissioner acknowledged this himself when he said at a hearing:

I get a lot of people saying to me: 'My kids used MyTax. It was fantastic.' I say, 'Why don't you?' They say: 'Oh, I don't know. Sounds a bit scary.' I think it is going to take a little while to get the migration of people into that.³⁸

6.55 The Black Economy Taskforce final report devotes considerable time to addressing identity crime concerns and on developing robust identity verification means. The report noted that: 'It has never been easier for criminals to obtain false identity papers or 'steal' another person's digital identity' and that 'in the 2015-16 financial year there was an 80 per cent increase in identity theft over the previous year'.³⁹ The Taskforce recommends 'a single individual identity to allow individuals to instantly and securely prove their identity using a digital identity credential, securely

³⁷ ATO Cyber-crime Warnings online, viewed 13 March 2018.

³⁸ Mr Chris Jordan AO, Commissioner of Taxation, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 8.

³⁹ *Black Economy Taskforce Interim Report*, March 2017, pp. 81, 82.

biometrically, when dealing with Government' and to strengthen the integrity of the ABN system.⁴⁰

6.56 People with simple tax affairs who have been paper self-lodgers are now expected to obtain, upgrade and maintain a reliable IT system at their own (non-deductible) cost and take all the risk of internet security exposure at their end to operate a myGov and myTax account. Otherwise, these people are obliged to employ a tax agent who, in 2009, almost a decade ago, charged on average \$206 for the cost of managing their tax affairs.⁴¹ The costs of managing tax affairs is tax deductible so for those on an average Australian wage they would be refunded approximately 32.5 per cent of this cost,⁴² but they would still need to meet the up-front costs for the service and the out-of-pocket cost of approximately \$139.

6.57 The Chief Digital Officer of the ATO admitted that he was concerned about disenfranchising and alienating some citizens. He said:

Another thing I would say is that I do lose sleep over the fact that, putting businesses aside, we do have a percentage of the population that will never get to digital. My mum will never get to digital. She has poor English skills. Her idea of a phone is she wants the old Nokia handset where you just ring or it rings like anything else.⁴³

6.58 This raises a significant point related to accessibility — those from non-English speaking backgrounds and with less proficient English skills may struggle to personally deal with their tax affairs, irrespective of the digital context, irrespective of how many years they have resided in Australia.

Maintaining privacy with digital engagement

6.59 The rise of digital engagement with the ATO also raises issues about maintaining privacy. As social media sites become more omnipresent, they provide considerable ground for governments to use as an information source to better understand the needs and behaviours of individuals and

⁴⁰ *Black Economy Taskforce Interim Report*, March 2017, pp. 81–86.

⁴¹ Australian Government, *AFTS Final Report, Part 2*, December 2009, vol. 1, p. 56.

⁴² The top marginal tax rate for an individual earning the average wage (AWOTE) of ~\$81 530 p.a. is 32.5 per cent (over \$37 000 and up to \$87 000).

⁴³ Mr John Dardo, Deputy Commissioner, Digital Delivery and Chief Digital Officer, ATO, *Committee Hansard*, Canberra, 27 October 2017, p. 25.

small businesses. The public are now starting to become aware or have a perception that governments are using social media in an intrusive way. This is leading to concerns regarding privacy breaches and perceived surveillance.

- 6.60 An Australian Broadcasting Corporation (ABC) article, in November 2016, warned that the ATO uses Facebook, Instagram and other social media to confirm the accuracy of information that is reported to it.⁴⁴ While this may not be entirely accurate, the general public were made aware that, in a high profile case of suspected tax crime uncovered in 2017, one method of identifying a pattern of unusual taxpayer behaviour involved viewing images posted to Facebook.⁴⁵
- 6.61 The Office of the Australian Information Commissioner (OAIC) conducts an annual survey of Australian attitudes to privacy. The 2017 *Australian Community Attitudes to Privacy Survey* (ACAPS) found ‘that sixty-nine per cent of Australians are more concerned about their online privacy than they were five years ago’.⁴⁶
- 6.62 The data also indicated that despite risks to privacy being of increased concern, Australians are not using or aware of basic privacy protections and rights. For example, the survey found, that the majority surveyed did not read the privacy policies of websites used and 43 per cent did not regularly adjust the privacy settings on their social media accounts.⁴⁷
- 6.63 Furthermore, approximately 25 per cent of those surveyed have rarely or never questioned an organisation why they need personal information, despite this being a basic privacy right; and 58 per cent were unaware they can request access to the personal information a business or government agency holds about them.⁴⁸
- 6.64 According to the survey, more than eight in ten (83 per cent) believed the privacy risks are greater when dealing with an organisation online

44 ATO Cyber-crime Warnings online, viewed 13 March 2018.

45 During Operation Elbrus, 2017.

46 J van Souwe, P gates, B Bishop, C Dunning, *The Australian Community Attitudes to Privacy Survey* (ACAPS)— 2017, Office of the Australian Information Commissioner (OAIC), <www.oaic.gov.au/engage-with-us/community-attitudes/australian-community-attitudes-to-privacy-survey-2017> viewed 6 November 2017.

47 ‘Commissioner’s Forward’, ACAPS—2017 [np].

48 ‘Commissioner’s Forward’, ACAPS— 2017, [np].

compared with other means. And yet, respondents were more relaxed about government holding their information than they were previously, with the trust differential widening for dealings with commercial entities.⁴⁹

- 6.65 In 2017 one in six (16 per cent) would avoid dealing with a government agency due to privacy concerns, with six in ten (58 per cent) avoiding dealing with a private company—a 42 point gap. By contrast, there was smaller gap of 37 points (23 per cent versus 60 per cent) in 2013.⁵⁰
- 6.66 Asked about the degree of trust given different types of organisations to look after their personal information, respondents indicated that Health service providers continue to be the most trusted organisations with eight in ten Australians (79 per cent) trusting them, followed by financial institutions (59 per cent), and government departments (58 per cent) respectively. Insurance companies (40 per cent) and charities (38 per cent) are trusted by four in ten.⁵¹ People aged under 35 were also significantly more likely than people aged over 55 to trust organisations of all types.⁵²
- 6.67 Similarly, on sharing of information—one third (34 per cent) of the community was comfortable with the government sharing their personal information with other government agencies. But only one in ten were comfortable with businesses sharing their information with other organisations.⁵³
- 6.68 While the Committee understands the enormous benefits both to the end user and government in the use of digital formats, these findings indicate that careful management of the transition to fully digital tax engagement processes and services must be a priority for the ATO. This would include conducting evaluations of taxpayer readiness to stage the process.

Recommendation 9

- 6.69 The Committee recommends that the ATO should adopt a roadmap for the abolition of paper-based returns, including testing and trialling with user groups.**

⁴⁹ 'Summary of Results', ACAPS 2017, p. i.

⁵⁰ 'Summary of Results', ACAPS 2017, p. i.

⁵¹ 'Summary of Results', ACAPS 2017, p. 8.

⁵² 'Summary of Results', ACAPS 2017, p. i.

⁵³ Summary of Results, ACAPS 2017, p. ii.

Recommendation 10

- 6.70 For the foreseeable future, the Committee recommends that the ATO maintain paper-based returns and the distribution of paper publications on request to those people who choose to engage this way.

Additionally, taxpayers seeking non-digital tax resources for tax returns at a myGov Shopfront should be assisted on site.

- 6.71 Tax forms and basic information packs should be available on site—or the inquirer added to a dynamic mailing list which enables a current tax return pack to be promptly posted to them.

Cyber resilience of the tax administrator

- 6.72 The rise of digital systems and other technological change raises ATO security issues, in particular the security of records held by the ATO. The ATO has prioritised internal data management as part of its commitment to deliver secure, stable and reliable online services to taxpayers using a range of authentication capabilities, and managed by a team dedicated to complete compliance and adherence to those capabilities.⁵⁴
- 6.73 The Committee sought information from the ATO as to the actions that it is taking to ensure security of information held and shared—in particular in relation to software providers and those connecting to a core ATO system.
- 6.74 The ATO's Chief Digital Officer provided a comprehensive overview of what is being considered and what is being developed—explaining the five elements of focus which include *certification, authentication, data sovereignty, the supply chain* and finally, *encryption*. He elaborated:

The first area is how you **certify or register a provider**, be it a software provider, mobile app provider or somebody who connects to our core systems. How do you certify them before you let them connect? What are the minimum standards they must have? How do we get that agreement?

The second area...is what **authentication** they must have at the front of their systems. If they just have password controls with no brute force protection that will be insufficient. So we are working through what they need to step up to on the front of their system. Whether you are a software provider or mobile

⁵⁴ Mr Ramez Katf, Chief Information Officer, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 4.

app, how do we know that you really do know your client and how do we know that that client really is who they say they are based on your controls?

The third one is...around **data sovereignty**. So if you do have data stored in an offshore location and are you a software provider, what assurances do we have that there is not sovereign risk to that data, that a local governor or a national body or the security agency of that country does not access that data at will?

The next...**the supply chain**...if you are a software developer and you have data in your systems, and you are letting that data be shared or used by other software developers and we cannot see that and your clients cannot see that, that is a risk.

The final area is **encryption**. When you get data, when you store data and when you move data, how do we encrypt it in all of those steps? What are the algorithms or the rules we have to encrypt the data so that even if somebody intercepts it, they cannot actually do anything with it?—What you may have to do is have rules that say it is encrypted between the points and the people that touch it are registered or whitelisted so that you have assurances that it is encrypted between, encrypted at rest and encrypted between again.⁵⁵

6.75 Asked about the incidence of breaches Mr Ramez Katf, the ATO's Chief Information Officer, said that he was not aware of any and further advised:

We have a very strong interest and investment in our cybersecurity holdings. We have a lot of people dedicated to that activity. Our cybercapability is multilayered. We have ISM compliance capabilities, we have authentication capabilities and we have a range of different vulnerabilities that we continue to address on a regular basis. It is one of our most important capabilities. We have quite a strong team focused on making sure that we have complete compliance and adherence to those capabilities.⁵⁶

6.76 The ATO also stressed that being cyber resilient and secure is a dynamic and ongoing challenge:

With regard to consultation, we will never finish this journey. What we have made really clear to developers, banks and super funds is that we will agree

⁵⁵ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, pp.18-19.

⁵⁶ Mr Ramez Katf, Chief Information Officer, ATO, *Committee Hansard*, Canberra, 29 March 2017, p. 4.

on a maturity framework. We will continue to have to escalate the requirements as malicious players continue to get more sophisticated.⁵⁷

6.77 To improve online security for the individual, the ATO has enabled more unique personal identifiers like voice imprint technology. The Commissioner of Taxation espoused the benefits of this new innovation, pointing out that the ATO is a pioneer in voice imprint for a transacting authorisation. He said:

By using your voice to authenticate your identity, when you say, 'In Australia my voice identifies me,' our app takes you to your own account and you can transact. You can put these figures in, you can make instalments, you can change your details, you can lodge your return, all through your smart device, using your voice to authenticate yourself. We in Australia are the first to enable anyone to transact. I think Citi, the American bank, brought it in after us, but we were the first to have voice authentication to transact. You have to go through myGov and link MyTax first, and then, when you download the app, it does ask you those questions to authenticate you that you would be asked in MyTax. But, once you leave your voice as a print, that is it; you can use that on the go, grab the stuff, chuck the receipt away—you are done.⁵⁸

6.78 However, Mr Jordan went on to lament:

...most people we talk to about it say, 'That is great. You should tell people about that.' It is often difficult to get mainstream publicity, mainstream exposure, for these good things that we are doing.'⁵⁹

6.79 The Committee sees that the ability of the ATO to manage the implementation of digital security systems as critical for the integrity of the tax system. It will also be important for the developers of tax law and the ATO as administrators of that law to identify and address potentially disruptive technology.

Emerging financial technology

6.80 Evidence was submitted to the inquiry about the potential impacts of new financial technology on the auditability of many transactions and how these might integrate into the tax system. These developments included new payment platforms, blockchain and digital currencies.

⁵⁷ Mr Dardo, ATO, *Committee Hansard*, Canberra, 27 October 2017, pp. 18–19.

⁵⁸ Mr Jordan, ATO, *Committee Hansard*, Canberra 29 March 2017, p. 3.

⁵⁹ Mr Jordan, ATO, *Committee Hansard*, Canberra 29 March 2017, p. 3.

New payment platforms

6.81 The Reserve Bank of Australia (RBA) announced the central bank's New (digital) Payment Platform (NPP) on 13 February 2018. The NPP allows for transactions between individuals or individuals and businesses or between businesses in real time.

6.82 The RBA Governor Philip Lowe stated at the launch:

The public launch of the NPP represents the delivery of a major piece of national infrastructure.

In particular, the NPP and the initial overlay service, Osko, will allow financial institutions to provide improved services to Australian businesses and consumers, including to:

- make real-time payments, with close to immediate funds availability to the recipient;
- make and receive payments on a 24/7 basis;
- have the capacity to send more complete remittance information with payments; and
- address payments in a relatively simple way.

Around 60 banks, credit unions and building societies will begin rolling out services to their customers from today, with the number of financial institutions and accounts linked to the NPP progressively increasing over the coming months.⁶⁰

6.83 The Committee heard from two independent platform providers about the new payments arena and the benefits of a strong regulatory framework—PayPal Australia is well established in the digital payments market, while Airwallex is a boutique payments provider start-up.

6.84 Paypal Australia noted that the integrity of its payment platform is critical and as such it invests heavily in data protection:

The essential element of the PayPal wallet is that the wallet holder can make payments or send funds to a third party, whether another PayPal account holder or a PayPal merchant, without ever disclosing to that other party the funding source that they have used for their payment. All financial data is encrypted and held by PayPal so that the source of funding is known only to the wallet holder and to PayPal. Trust in the efficacy, security and certainty of

⁶⁰ RBA, *Media Release*, 'Launch of the New Payments Platform', 13 February 2017.

our product and associated services is at the heart of our customer and merchant value proposition.⁶¹

- 6.85 Significantly, Paypal operates a system based on trust, security and certainty, despite the massive volume of transactions processed through the platform. Mr Simon Edwards, Director, Government Relations, reported on the quantum of this data—and the rise of cashless transactions using mobile networks:

To give you an idea of the scale of this business, in the June quarter of this year PayPal processed 1.8 billion transactions worth in excess of \$106 billion US dollars. Importantly, in the same quarter, the average number of transactions per PayPal active account user increased to 32.3, which represented a 10 per cent increase over the previous year, and the volume of mobile payments on our platform increased by more than 50 per cent, accounting for a third of all payments made using PayPal.⁶²

- 6.86 As mentioned in Chapter 5, the ATO has noted that even though digital systems can potentially identify any data, the Tax Office is not envisaging the NPP as a data gleaning mechanism:

We see that the NPP will be able to facilitate interactions. The overlay services that sit over the top of that and/or the identity requirements that sit in it are something for government and/or industry to really work through. I imagine that there will be a range of discussions about what may or may not sit in the NPP.⁶³

- 6.87 At a hearing in Canberra, Dr Anthony Richards, Head of Payments, RBA clarified the benefits that the NPP could bring:

The NPP has been designed as a platform for innovation that will benefit end users of the payments system—households, businesses and government entities. One key feature that will facilitate new services will be the ability to include much more data with the payment—up to 280 characters of data as opposed to the current limitation of just 18 characters in the direct entry system. Richer data will facilitate e-invoicing and straight through processing

⁶¹ Mr Simon Edwards, Director, Government Relations, Paypal Australia, *Committee Hansard*, Canberra, 16 August 2017, p. 2.

⁶² Mr Simon Edwards, Director, Government Relations, Paypal Australia, *Committee Hansard*, Canberra, 16 August 2017, p. 2.

⁶³ Mr Dardo, ATO, *Committee Hansard*, 27 October 2017, p. 23.

and is likely to offer enhanced functionality to government agencies, including those under the DHS umbrella.⁶⁴

6.88 Besides real time 24/7 operation, this is the significant benefit of the NPP—the rich data abilities which will enable business-to-business invoicing information which benefits businesses in the data flow to other agencies, like the ATO, in the course of a natural business function. This means no duplicated effort and its simplicity aids willing participation in the tax system and reduces compliance costs.

6.89 The greatest hurdle for tax administration in the current fintech space is that the data may be rich but it is voluminous. The Attorney-General's Mr Daniel Mossop, Director, Financial Crime Section, referred to the technical challenges imposed by Fintech innovations:

The pace of innovation in that space is a constant challenge, in terms of capturing those transactions, particularly in a way that provides intelligence to law enforcement and national security agencies, but also one that provides some level of oversight for the ATO.⁶⁵

6.90 Mr Edwards of Pay Pal Australia recommended:

As the private sector drives momentum towards digital payments, governments can, in my view, do a number of things:

- 1 support the further development of a digital applications industry;
- 2 give consideration to the governance of data sharing by government agencies such as to advance public interest while substantially recognising and protecting both individual privacy rights and the concept of a free society;
- 3 build upon the NPP, with government payments in real time utilising popular consumer payment systems;
- 4 support Australian online retailers selling to the world by considering regulatory actions in the context of the global market—for example, to review and revise international tax agreements for the digital age that reflect digital commerce—; and

⁶⁴ Dr Anthony Richards, Head of Payments Policy, RBA, *Committee Hansard*, Canberra, 27 October 2017, p. 30.

⁶⁵ Mr Daniel Mossop, Director, Financial Crime Section, Attorney General's Department, *Committee Hansard*, Canberra, 21 June 2017, p. 4.

- 5 develop internationally consistent regulation in data privacy, security and, ultimately, taxation to enable global trade at the lowest possible transaction cost. In this regard, I would specifically call out the need for the development of a digital identity for companies, businesses and individuals.⁶⁶

- 6.91 The ATO stated in a supplementary submission that it ‘looks to identify potential future developments (including technologies) that might impact the tax and super system’.⁶⁷ The submission also states that the ATO has been in discussion with a number of technology and advisory providers to ‘explore the potential for emerging payment technologies to enhance aspects of administration of the tax and super system’.⁶⁸
- 6.92 The Committee does not believe these transaction platforms pose a large problem for tax compliance at this stage because most of the transactions occur through platforms with links to financial institutions from which the ATO can access data. Issues may arise in the future as the volume of transactions increases, or if the ATO was unable to access information about these transactions.

Blockchain

- 6.93 Blockchain is an electronic distributed ledger system that enables unique identifiers of transactions that are secure and robust to potential manipulation. The ledgers are generally public.
- 6.94 The evidence to this inquiry is that the transparent nature of the ledgers means that they are unlikely to pose a significant risk for tax administrators as the ATO will be theoretically able to observe transactions and the ledgers may even have a positive use within the tax system.⁶⁹
- 6.95 Mr Mossop of the Attorney-General’s Department believes:

I think theoretically there are a lot of advantages for blockchain and distributed ledger technology as a single immutable source of truth. That might have benefits in some areas of law enforcement, where you might have

⁶⁶ Mr Simon Edwards, Government Relations, PayPal, *Committee Hansard*, Canberra, 16 August 2017, p. 3.

⁶⁷ ATO, *Supplementary Submission 15.2*, p. 11.

⁶⁸ ATO, *Supplementary Submission 15.2*, p. 11.

⁶⁹ Dr Chris Berg, Private capacity, *Committee Hansard*, 18 October 2017, pp. 1–2

registries that are more difficult to dupe or verification can occur at the time of entry.⁷⁰

6.96 The significance of the blockchain from a current tax perspective is that it forms the foundation for the transacting of most cryptocurrencies, famously for bitcoin, discussion of which follows. All the computers in the blockchain network repeatedly agree that the distributed ledger is true by using an algorithm called a consensus mechanism.⁷¹ This process uses enormous amounts of electricity. This has led some to believe the blockchain concept will have a limited commercial use for asset or data management at this stage until a less energy hungry method of verifying the blockchain is developed.

6.97 However, Dr Chris Berg, in his private capacity, said at a hearing in Canberra that:

Blockchains are likely to bring about enormous changes to the way we work. For now, though, and to conclude, we'll leave it that any use of new digital technology for government revenue has to place fundamental values, like privacy and the rule of law, at the centre.⁷²

6.98 Dr Berg also opined the potential benefits of blockchain in audit and tax administration:

...blockchain applications make things like real-time reporting and payment of tax obligations possible. A large public company, for instance, could place its accounts on a publicly verifiable blockchain, substantially reducing or eliminating the need for auditors. We're not proposing requiring real-time blockchain reporting as a regulatory requirement, but we would urge shareholders in public companies to consider demanding this of management. We can also see some attractions for small- and medium-sized firms of real-time blockchain reporting, as this would automate tax compliance and make business activity statements redundant. The ATO, in our view, should develop guidelines for real-time blockchain reporting that it would consider to be reasonably compliant.⁷³

⁷⁰ Mr Mossop, Attorney-General's Department, *Committee Hansard*, 21 June 2017, p. 7.

⁷¹ When this occurs in a blockchain supporting a cryptocurrency it is referred to as 'mining' the cryptocurrency.

⁷² Dr Chris Berg, Private capacity, *Committee Hansard*, 18 October 2017, pp. 1-2.

⁷³ Dr Berg, Private Capacity, *Committee Hansard*, Canberra, 18 October 2017, pp. 1-2.

6.99 Mr Edwards of Paypal Australia raised what he believes is the most critical issue surrounding the advancement of all online digital activity — that of secure identification mechanisms in the system. He noted that one of the potential options for the use of blockchain to validate identity:

This is an international issue. It is one that the private sector is looking at worldwide. It is one that governments are looking at worldwide. I'm aware that within the Australian government today there are a number of agencies that are trying to look at how do this. This is the fundamental issue to crack. You will have probably been advised already in terms of the notion of blockchain technologies. Fundamentally, this concept of identity is at the heart of what blockchain is trying to overcome or the problem it is trying to resolve.⁷⁴

6.100 Mr Alistair MacGibbon, the Prime Minister's Special Adviser on Cybersecurity, at a hearing in Canberra clarified — significantly — that although the validity of the Bitcoin in a blockchain register may be verified, the identity of the owner or owners is not, which would be a fundamental issue for taxation matters:

It does not track back to me in particular; it just says that this bitcoin is a bitcoin. It does not say that it used to be owned by Alastair MacGibbon, and now it is passed to Jason. But it says that it is a bitcoin.⁷⁵

6.101 Further, Mr MacGibbon elaborated:

There is a dark web that is not searchable by our favourite search engines; you need to specifically go to it using browser technologies — Tor technologies, onion routers — to get to these websites. So only someone with particular bits of software on their computer can get to it, and then you can transact in ways that are not observable.⁷⁶

6.102 Similarly, the Governor of the RBA Dr Lowe raised the need to develop a strong identity and authorisation system in the financial sector as key areas to be resolved in a timely manner. He preferred non-regulatory resolution

⁷⁴ Mr Simon Edwards, Director, Government Relations, PayPal Australia, *Committee Hansard*, Canberra, 16 August 2017, p. 4.

⁷⁵ Mr Alistair MacGibbon, Special Adviser to the Prime Minister on Security, Department of the Prime Minister and Cabinet, *Committee Hansard*, Canberra, 10 May 2017, p. 11.

⁷⁶ Mr Alistair MacGibbon, *Committee Hansard*, Canberra, 10 May 2017, p. 11.

by industry participants, but failing that, the Payments Board 'would need to consider what steps it might take to promote the public interest'.⁷⁷

Digital currencies

- 6.103 Digital, electronic or cyber-currencies act in a similar way to paper money only they are electronic and generally involve the transfer of tokens to enable the transactions. The most well-known of these, Bitcoin, is enabled through the new technology medium of blockchain, discussed above.
- 6.104 These currencies pose a risk to tax compliance to the extent that their use can be hidden through private facilitators of the currency, in a similar way that paper cash transaction can be hidden from tax agencies, enabling money laundering on a significant scale. This was mentioned in Chapter 5.
- 6.105 The ATO provides considerable guidance on the current tax treatment of digital currencies, in particular Bitcoin, on its website, with information current as at 16 March 2018. Prior to the update on 16 March 2018 the 21 December 2017 information particularly referred to Bitcoin. It noted that Bitcoin operates like a barter system, with similar tax consequences. The ATO website now states that:

Our view is that Bitcoin is neither money nor a foreign currency, and the supply of Bitcoin is not a financial supply for goods and services tax (GST) purposes. Bitcoin is, however, an asset for capital gains tax (CGT) purposes.

You need to keep the following records for cryptocurrency transactions:

- the date of the transactions;
- the amount in Australian dollars (which can be taken from a reputable online exchange);
- what the transaction was for;
- who the other party was (even if it's just their bitcoin address).⁷⁸

- 6.106 Furthermore, it states that where you use Bitcoin for personal transactions there will be no income tax or GST implications and also any capital gain or

⁷⁷ Governor Philip Lowe, Reserve Bank of Australia (RBA), 'An eAUD?', Address to the Australian Payment Summit Sydney, 13 December 2017.

⁷⁸ Refer ATO website: *Tax Treatment of Crypto-Currencies in Australia—Specifically Bitcoin, Transacting with Bitcoin*, See < www.ato.gov.au/General/Gen/Tax-treatment-of-crypto-currencies-in-Australia---specifically-bitcoin/> viewed 21 December 2017, but note: updated on 16 March 2017 to change all references from 'barter' to 'property'.

loss will be disregarded as it will be treated as a personal use asset (unless it exceeds A\$10 000). A business receiving bitcoin, however, will need to recognise that transaction in Australian dollars as part of ordinary income using a fair market exchange value at a reputable bitcoin exchange dealer. This recording process is the same process as receiving non-cash consideration under a barter transaction.⁷⁹

6.107 It appears to be the case that the trail of ownership and exchange will eventually rely on the data stored in the underlying blockchain ledger to test the voracity of taxpayer records. Given that cryptocurrency data is not currently regulated, and any means of the ATO being able to access it, as third party data, and then decipher the information in any efficient and meaningful way will be the key to taxpayer engagement in this market.

6.108 On 27 October 2017, the RBA's Dr Richards echoed this, saying:

The use of bitcoin and other digital currencies as an actual method of payment remains relatively limited in Australia, as elsewhere. From the bank's payments policy mandate, digital currencies do not currently appear to raise any pressing regulatory issues. As you noted earlier, cryptocurrencies can serve as a means of payment in the illicit economy. Accordingly, their use may have some implications for tax authorities. They raise more significant issues for authorities tasked with crime prevention and detection. The distributed and cross-border nature of digital currencies like bitcoin means that regulation of the core protocols of these systems is unlikely to be effective. Authorities have therefore tended to focus on the on-ramps or the off-ramps—that is, the links to the traditional payments system. In some jurisdictions, central banks and other authorities have taken action in relation to digital currency exchanges, such as the measures taken by the People's Bank of China earlier this year.⁸⁰

6.109 While the Committee took a significant amount of evidence speculating on the potential risks of digital currency, the Committee has also noted recent advice from RBA Governor Dr Lowe, that the use of these currencies is very low now and is likely to stay so.⁸¹

⁷⁹ Refer ATO website: *Tax Treatment of Crypto-Currencies in Australia—Specifically Bitcoin, Transacting with Bitcoin*, 21 December 2017, viewed 12 March 2018.

⁸⁰ Dr Richards, RBA, *Committee Hansard*, Canberra, 27 October 2017.

⁸¹ Governor Lowe, RBA, 'An eAUD?', Address to the Australian Payment Summit Sydney, 13 December 2017.

6.110 It is clear that in future, Governments will, however, need to ensure that tax regulators are able to audit these currency providers. Commenting on this during the inquiry, Mr Mossop of the Attorney-General's Department reported:

The reality for us is that it is not a good medium. You cannot live in the digital currency economy. You can probably buy a coffee at a trendy cafe in Melbourne but there is not a lot that you can do. You cannot buy groceries from Woolworths or buy a car. By and large, you cannot do that in bitcoin yet, so you cannot live in that digital currency world. At some stage, you need to cash it in or cash it out. But, as that progresses, the availability of retailers and average shops or retailers who will take that type of currency may increase. And then it starts to become a bit more of an issue.

That is something we are considering, at the moment, and we are looking at reforms to bring those digital currency exchanges, the on ramps and off ramps—where you would change it for real-world currency, fiat currency, into the AML regime so that people are identified and that gets reported to AUSTRAC. This is so there is some oversight when people are coming on or off the digital currency, out of the digital currency world.⁸²

6.111 Mr Mossop made a significant point about the future of exchange (essentially in a product you can't see or touch and which has no value in terms of sustenance, comfort or shelter—products used in traditional forms of barter). This would indicate that a cryptocurrency will either eventually need to be cashed out and thus the potentially significant tax implications to be considered—or lose its underlying 'market' value and as such become a low value or worthless product, potentially with loss impacts in the magnitude of losses currently recognised as 'cyber scams'.

6.112 Similarly, Dr Richards of the RBA stated:

Households seem very content to leave their transactions balances and their savings in commercial banks, building societies and credit unions. In large part, this may reflect the protection that they know they have from the Financial Claims Scheme. It is possible to see a world where households choose to keep some of their transaction balances outside of those accounts, but I struggle to see a world where they would be comfortable holding large amounts of their balances in, for example, non-guaranteed systems.⁸³

⁸² Mr Mossop, Attorney-General's Department, *Committee Hansard*, Canberra, 21 June 2017, p. 4.

⁸³ Dr Anthony Richards, Head of Payments, RBA, *Committee Hansard*, Canberra, 27 October 2017, p. 31.

- 6.113 The Committee notes there appears to be a high degree of uncertainty surrounding the tax treatment of cryptocurrencies. The Committee noted the change of definition of Bitcoin and Bitcoin transactions as described by the ATO per website advice on 21 December 2017 and then updated on 16 March 2018 (with no preceding reference or detail of what the change meant in practice). Furthermore, the ATO website advises that the ATO is currently consulting with industry and inviting feedback on 'practical compliance issues arising from cryptocurrency to cryptocurrency transactions'. The consultation closing date through the 'Let's Talk' medium was 20 April 2018.
- 6.114 The Committee sees this area of taxpayer engagement as evolving and notes that it requires a watchful eye by the tax administrator and financial regulators.

Committee conclusion

- 6.115 It is evident that to meet the current and emerging challenges of a 21st century tax system the ATO cannot operate as an administration, collection and enforcement agency in isolation. It must also be a collaborator to strengthen, protect and maintain the security and integrity of the tax system—and the control and access to highly sensitive data.
- 6.116 The biggest threat to the operation of digitised transaction, recording and reporting systems, and benefits accruing from single step processes for multiple functions, is weak security and poor authentication measures in those systems. The ATO is investing in maintaining digital security and while the committee is not in a position to provide an evaluation or audit of these investments, it appears that these investments and the processes around digital security within the ATO are sound at this stage.
- 6.117 At an operational level, while the ATO is confident that the service outages affecting its business over December 2016 and February 2017 have led to a more resilient and reliable digital platform, concerns in the community, in particular among tax professionals, means that maintaining utterly reliable and efficient tax services for all community sectors will remain a priority and a challenge for the ATO well into the future.
- 6.118 Reports during the inquiry that the ATO is not listening to businesses who must carry lengthy downtimes for regular ATO system upgrades and maintenance, of distress to individuals subject to debt allegations which result from data error, or to individuals who have failed to comply because they simply do not understand what is required of them or, again, to people

in the community who, for whatever reason, are not prepared for digital engagement, suggests the ATO must respond.

- 6.119 As discussed early in this report, the ATO is cognisant of the connection between confidence and trust and the voluntary compliance of taxpayers. Trust develops from accountability and from the taxpayer's confidence that he or she will receive fair treatment from the tax administrator under the law.
- 6.120 The ATO's effective management of taxpayers personal data will be vital not only to maintain taxpayers' confidence in data collection but also to the operation of the tax system overall. The Committee believes that this will become an increasingly important issue into the future and that, therefore, the rights and obligations of both parties within the tax engagement process should be now be clearly defined.

Recommendation 11

- 6.121 In the interests of promoting fairness and taxpayer confidence in Australia's tax system, the Committee recommends that the ATO should work to develop a framework which clearly outlines the rights and obligations of both parties in the tax engagement process for adoption in the near future.**

The process, involving the review of high level ATO mission statements, would be consistent with the ATO's principle-based approach to service delivery and support design of a Regulatory Philosophy document.

Recommendation 12

- 6.122 The Committee also recommends that, in implementation and change management programs, the ATO should include a service level agreement with end users, especially tax agents, that includes amongst other things, consideration of payments to end users for poor delivery outcomes.**

This is proposed in recognition that the ATO is a monopoly provider that is not subject to contestability in its service delivery.

- 6.123 In this regard, the Committee reiterates its view that the ATO should treat all providers in the tax engagement process according to the principal of competitive neutrality, so that taxpayers can access tax services and supports in the most suitable way to meet their needs.

Recommendation 13

6.124 The Committee recommends that the ATO should engage with all service providers according to the principle of competitive neutrality, allowing taxpayers the ultimate choice of which channel of access or service to use, and which channel is in their best interests.

Mr Jason Falinski MP

Chair

A. Submissions

- 1 Professor Michael Blissenden
- 2 Institute of Public Accountants
- 3 Chartered Accountants Australia and New Zealand
- 4 CPA Australia
- 5 Inspector-General of Taxation
- 6 Mr Richard Highfield
- 7 Australian Taxpayers' Alliance
 - 7.1 Supplementary
- 8 Community and Public Sector Union
- 9 Tax Practitioners Board
- 10 Australian National Audit Office
- 11 The Treasury
- 12 Tax and Super Australia
 - 12.1 Supplementary
- 13 Attorney-General's Department
- 14 Mr John Broomhead — *Content withheld*
- 15 Australian Taxation Office

- 15.1 Supplementary
 - 15.2 Supplementary
- 16** The Tax Institute
- 16.1 Supplementary
- 17** Board of Taxation
- 18** Department of the Prime Minister and Cabinet
- 19** Etax Accountants
- 20** Dr Toni Chardon, Prof Mark Brimble and Dr Brett Freudenberg
- 21** Mr Pier Parisi
- 22** ECU Australia Ltd
- 23** Professor Helen Anderson
- 24** George Abernathy
- 25** Council of Small Business Australia
- 26** Australian Securities & Investments Commission

B. Exhibits

1 Airwallex Pty Ltd

Ms Jasmine Koh, General Counsel
Airwallex—Presentation, 18 July 2018

2 *YourLifeChoices*

YourLifeChoices, Tax Survey Analysis, 12–18 July 2017

3 Chartered Accountants Australia and New Zealand

M Taylor et al, *Good Work—the Taylor Review of Modern Working Practice*, An independent review of modern working practices by the Chief Executive, Royal Society of Arts, 11 July 2017

4 Australian Taxpayers' Alliance

M Sinclair, 'Competitive Company Taxes', Europe Economics [nd]

5 Reserve Bank of Australia

Transactions Per Capita—Rolling Annual Sum 1997–2017
27 October 2017

C. Public hearings

Wednesday, 29 March 2017

Parliament House, Canberra

Australian Taxation Office

- Mr Chris Jordan AO, Commissioner of Taxation
- Mr Ramez Katf, Chief Information Officer
- Mr Neil Olesen, Second Commissioner
- Ms Emma Rosenzweig, Acting Deputy Commissioner
- Ms Melinda Smith, Chief Service Delivery Officer

The Treasury

- Mr Philip Akroyd, Senior Adviser
- Mr Graeme Davis, Acting Division Head

Wednesday, 10 May 2017

Parliament House, Canberra

Inspector-General of Taxation

- Mr Duy Dam, Acting General Manager
- Mr Andrew McLoughlin, Deputy Inspector-General of Taxation
- Mr Ali Noroozi, Inspector-General of Taxation

Department of the Prime Minister and Cabinet

- Professor Michael Hiscox, Director, Behavioural Economics Team of the Australian Government
- Ms Amanda Kingston, Senior Advisor, Projects, Behavioural Economics Team of the Australian Government
- Mr Alastair MacGibbon, Special Adviser to the Prime Minister on Cyber Security
- Ms Tara Oliver, Managing Director, Behavioural Economics Team of the Australian Government

Wednesday, 24 May 2017

Parliament House, Canberra

Australian National Audit Office

- Mr Tom Ioannou, Acting Deputy Auditor-General

Australian National Audit Office

- Mr Andrew Morris, Executive Director, Performance Audit Services Group

Wednesday, 14 June 2017

Parliament House, Canberra

*Mr Richard Highfield, Private capacity***Wednesday, 21 June 2017**

Parliament House, Canberra

Attorney-General's Department

- Mr Adrian Breen, Assistant Secretary, Transnational Crime Branch
- Mr Daniel Mossop, Director, Financial Crime Section

Australian Criminal Intelligence Commission (ACIC)

- Mr David Ross, Head of Determination, Targeting Criminal Wealth

Australian Transaction Reports and Analysis Centre (AUSTRAC)

- Mr David Hawkins, A/g National Manager, Strategic Intelligence and Policy

Monday, 17 July 2017

Commonwealth Parliament Offices

1 Bligh Street, Sydney

Chartered Accountants Australia and New Zealand

- Mr Michael Croker, Tax Leader, Australia
- Mr Peter Vial, New Zealand Country Head and Tax Leader

Behavioural Insights Team UK – Sydney Office

- Mr Edward Bradon, Senior Advisor
- Dr Rory Gallagher, Managing Director, Asia-Pacific

Board of Taxation

- Ms Karen Payne, Chief Executive Officer and Board Member

CPSU

- Mr Osmond Chiu, Policy and Research Officer
- Mr Michael Tull, Assistant National Secretary

Private Capacity

- Professor Robert Slonim

E-Tax

- Mr Ken Thomas, General Manager

Australian Taxpayers' Alliance

- Mr Alex Cullen, Research Associate

Tuesday, 18 July 2017

Parliament of Victoria

55 St Andrews Place, East Melbourne

Institute of Public Accountants

- Mr Tony Greco, General Manager, Technical Policy

CPA Australia

- Mr Paul Drum, Head of Policy

Airwallex

- Ms Jasmine Koh, General Counsel
- Mr Joe McGuire, Global Head of Sales and Partnerships

Tax and Super Australia

- Mr David Ebdon, Tax Specialist, Technical Services

Private Capacity

- Professor Helen Anderson

Your Life Choices

- Ms Kaye Fallick, Publisher
- Mr Drew Patchell, Digital Operations Manager

Wednesday, 16 August 2017

Parliament House, Canberra

PayPal Australia

- Mr Simon Edwards, Director, Government Relations

Council of Small Business Australia

- Mr Peter Strong, Chief Executive Officer

Wednesday, 6 September 2017

Parliament House, Canberra

(Teleconference)

The Tax Institute

- Ms Stephanie Caredes, Tax Counsel
- Mr Matthew Pawson, President

Wednesday, 13 September 2017

Parliament House, Canberra

The Australian Small Business and Family Enterprise Ombudsman (ASBFEO)

- Mr Craig Latham, Deputy Ombudsman
- Mr James Strachan, Director Advocacy

Wednesday, 18 October 2017

Parliament House, Canberra

Private Capacity

- Dr Christopher Berg

Private Capacity

- Professor Sinclair Davidson

Wednesday, 25 October 2017

Parliament House, Canberra

Master Grocers Australia

- Mr Jos de Bruin, Chief Executive Officer
- Ms Carmel Goldsmith, Member

Australian Retailers Association

- Mr Michael Heath, Director Policy, Government and Corporate Affairs
- Mr Rohan Pike, Illicit Trade Adviser

Friday, 27 October 2017

Parliament House, Canberra

Xero Australia Pty Ltd

- Mr Matthew Prouse, Partner Solutions Manager

MYOB Australia Pty Ltd

- Mr Timothy Reed, CEO
- Mr David Weickhardt, General Manager

Australian Taxation Office

- Mr John Dardo, Deputy Commissioner, Digital Delivery, and Chief Digital Officer
- Ms Annie Ferguson, Assistant Commissioner, Individuals Service Centres
- Ms Emma Rosenzweig, Assistant Commissioner, Experience, Strategy and Governance

- Mr Andrew Watson, Assistant Commissioner, Tax Practitioner Digital Service

Reserve Bank of Australia

- Dr Anthony Richards, Head, Payments Policy Department
- Mr David Emery, Senior Manager, Payments System Efficiency, Payments Policy Department

Digital Transformation Agency

- Mr Peter Alexander, Chief Digital Officer

**D. Extract from Submission 17 -
Annexure A - Board of Taxation**

Annexure A - The Overseas Experience

A number of international jurisdictions have responded to the threat posed by the shadow economy. The following outlines a selection of methods that have been implemented (or are planned to be implemented) by tax administrators and law-makers overseas²:

Jurisdiction	Methods
France	Cash payments of over 1000 Euros have been banned for French citizens, as well as cash payments of over 10,000 Euros for foreign citizens.
Denmark	Established a goal of eradicating cash by 2030. Likely to be followed in other Nordic countries (entirely cashless societies).
Spain	<p>The Spanish Tax Office has increased its use of data analytics to analyse and cross-reference various forms of electronic information to detect and prevent tax fraud, including using information supplied by utility companies to ascertain whether a premises is actually being used for its stated purpose.</p> <p>Cash payments over 2,500 Euros are prohibited when at least one of the parties to a transaction is a company or a professional.</p> <p>The names of taxpayers with more than one million Euros of tax debt are now published in a list and anyone convicted of tax offences has their identity published in the daily Spanish Official Gazette.</p> <p>Spanish Tax Office has also begun offering bonuses to its staff for meeting tax fraud detection targets.</p>
Italy	<p>Italian Police have conducted “spot-audits” on owners of luxury vehicles (such as Ferraris and Bentleys) to collect data on their owners and cross-check them with declared income.</p> <p>The Government closed some well-known tax loopholes by requiring banks to transfer data to tax authorities, resulting in a wave of audits.</p> <p>Government also struck an information sharing deal with the Government of Switzerland in 2015 which offers a partial tax amnesty to Italians that have hidden cash in Switzerland.</p>
Greece	The Government entered into exchange of information agreements with a number of countries as part of the Organisation for Economic Development’s Base Erosion and Profit Shifting (BEPS) plan. In addition, the Government entered into specific agreements with Germany to bolster its expertise on tax collections.

² The information included in Annexure A was collated as preliminary research for project scoping purposes only and has not been verified with the relevant foreign governments or their agencies. Accordingly the Board cannot confirm or guarantee what action has been taken to implement these proposals or initiatives.

Jurisdiction	Methods
Sweden	<p>Staff ledgers at commercial construction sites will keep information on all employees present at the site (including contractors) and be subject to unannounced inspections by the Swedish Tax Agency (STA).</p> <p>New legislation will come into force in 2017 requiring all data from mandatory taximeters to be stored at designated commercial third party central repositories, to which the STA will have on-demand access.</p> <p>Since 2010, businesses selling goods and services in return for cash payments must have a certified cash register (“black-box”) which provides real-time information to the STA on the business’ activities.</p>
Norway	<p>Individual’s tax returns are posted online annual and available for public inspection (notice is provided to an individual where another individual checks their data, however inspections by Norwegian media will not prompt any notice).</p>
Hong Kong	<p>Increasing the types of vendors and service providers who accept the electronic “Octopus” contactless smart card (now includes transport, retail, parking, online-payments, self-service kiosks and public services), thereby further reducing the need for cash transactions.</p>
Portugal	<p>The Government organised a lottery in 2014 for people who demanded receipts for goods and services they purchased, with prizes including Audi motor vehicles.</p>
India	<p>The Government is working toward policies to encourage non-cash payments.</p> <p>The Government is also seeking to introduce a broad-based Goods and Services Tax (GST) that would also extend to e-commerce.</p>
United Kingdom	<p>Her Majesty’s Revenue and Customs (HMRC) has used a variety of publicity campaigns to encourage people to report undeclared income.</p> <p>HMRC also recently gained greater powers to obtain data from payment providers and businesses intermediaries to identify hidden economic activity.</p> <p>HMRC is currently consulting on making access to licenses or services for businesses conditional on being registered for tax and for new sanctions to be applied to those who repeatedly and deliberately participate in the hidden economy, including penalties and monitoring of repeat offenders.</p>
Canada	<p>The Canadian Revenue Agency (CRA) is refining their understanding of the shadow economy and seeking to reduce the social acceptability of participation in the shadow economy.</p> <p>The CRA also established an ‘Underground Economy Advisory Committee’, comprising representatives from key industry stakeholder organisations representing a cross-section of Canadian businesses and tax professions) to provide the Minister for National Revenue with direct access to industry perspectives/input</p>

Jurisdiction	Methods
	to help inform the strategy for tackling the underground economy.
United States of America	<p>The Internal Revenue Service (IRS) employ specific auditing techniques when targeting businesses they suspect are operating the shadow economy, including undertaking comparative analyses of assets and interests, researching civil, criminal and family court files and examining loan application documents.</p> <p>IRS initiatives offering amnesty in exchange for voluntary disclosures of tax non-compliance are also used extensively.</p> <p>The US Government passed legislation in 2012 strengthening transparency and accountability of electronic payment service providers in the US.</p>
New Zealand	<p>New Zealand Inland Revenue (NZIR) investing in a specific “Hidden Economy” programme, complete with national marketing campaigns (“e.g. Declare it all or risk everything” and “Crackdown on Cashies”) targeting specific industries and raising awareness of the consequences of businesses avoiding tax obligations.</p> <p>NZIR developing and enhancing relationships with local and national participants and stakeholders in specific industries on the importance of paying taxes, recording transactions, providing receipts and requesting invoices.</p> <p>NZIR also encouraging anonymous whistleblowing on shadow economy activity.</p>

Extract from Annexure A of Submission 17 – Board of Taxation

E. International Work Related Expense (WRE) Deductions

Box A1–2: International comparisons of deductions for WREs

Country	Deductions for work-related expenses	Scope of deductions and arrangements
Australia	Yes	Incurred in gaining or producing an employee's assessable income.
Canada	Limited	Only deductions specifically legislated are allowed, including accounting and legal fees.
Denmark	Yes	Wage or salary earners can fully deduct work-related expenses from income, after a standard deduction has been applied.
Ireland	Yes — narrow	Expenses incurred wholly, exclusively and necessarily in the performance of duties.
Japan	Limited	Specific deductions that exceed the standard deduction for employment income are allowed. Specific deductions include travelling expenses.
Netherlands	Yes — narrow	Most work-related expenses are not deductible; in limited circumstances exceptions apply for transport, education and home office expenses. There is an employed person's tax credit.
New Zealand	No	No deductions for work-related expenses for employees.
Spain	No	Expenses relating to employment are generally not deductible. Some exceptions include trade union / professional association fees and legal expenses on termination. Other allowances and a standard deduction are available.
Switzerland	Yes — narrow	Necessary work-related expenses are deductible — 3 per cent of net income with a minimum and maximum deduction.
United Kingdom	Yes — narrow	Most claimable expenses must be incurred wholly, exclusively and necessarily in the performance of an employee's duties, a condition that precludes the deduction of many employment-related expenses.
United States	Limited	Employees can deduct work-related expenses subject to limits (expenses generally only deductible to the extent they exceed 2 per cent of adjusted gross income). Taxpayers have the option of claiming a standard deduction in lieu of itemising deductions.

Source: Adapted and updated from *International comparison of Australia's taxes* released April 2006, OECD *Taxing Wages 2007–08* and International Fiscal Database Documentation.

Source: Submission 6, Annex 2, p. 25 from — *Australia's Future Tax System—Report to the Treasurer, May 2010, Part 2, Volume 1, p. 54.*